Supreme Court, U.S.
FILED
JAN 13 1992
OFFICE OF THE CLERK

No. 91-1135

IN THE

Supreme Court of the United States

OCTOBER TERM, 1991

NEWARK MORNING LEDGER CO.,
as successor to The Herald Company,
Petitioner,

v.

UNITED STATES OF AMERICA,
Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

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QUESTION PRESENTED

1. Whether the Third Circuit, in acknowledged conflict with other circuits and the United States Tax Court, was correct that under the Internal Revenue Code an income-producing wasting intangible asset may be nondepreciable "goodwill" as a matter of law.

PARTIES TO THE PROCEEDING

Petitioner, plaintiff in the district court and appellee in the court of appeals, is Newark Morning Ledger Co.* Respondent is the United States of America.

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* The parent company of petitioner Newark Morning Ledger Co. is Advance Publications, Inc. Subsidiaries or companies in which Newark Morning Ledger Co. owns a significant interest (other than wholly owned subsidiaries) are Crown Outlet Holding Corp., Business People Publications Limited, Condé Nast and National Magazine Distributors Limited, Wagadon Limited, Barrie & Jenkins Limited, Frampton Flora Limited, Triad Paperbacks Limited, Constable & Company Limited, Watchword plc, Andersen Press Limited, and Vision Cable of Pinellas, Inc.

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UNITED STATES OF AMERICA,
Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

Newark Morning Ledger Co. hereby petitions for a writ of certiorari to review the judgment of the United States Court of Appeals for the Third Circuit in this case.

OPINIONS BELOW

The opinion of the Third Circuit, as amended, is reported at 945 F.2d 555 (3d Cir. 1991), and is reprinted in the Appendix hereto at 1a-30a.[1] The opinion of the United States District Court for the District of New Jersey is reported at 734 F. Supp. 176 (D. N. J. 1990), and is reprinted in the Appendix at 31a-51a.

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[1] References to the Appendix to this Petition are cited herein as "App. at ___ a."

JURISDICTION

The judgment of the Third Circuit was entered on September 12, 1991. Rehearing *en banc* was denied (Circuit Judges Greenberg and Nygaard dissenting) on October 15, 1991. (App. at 52a-53a). The Third Circuit stayed its mandate on November 14, 1991. This Court has jurisdiction pursuant to 28 U.S.C. § 1254(1).

STATUTE AND REGULATION INVOLVED

Section 167 of the Internal Revenue Code states in relevant part:

> (a) GENERAL RULE.—There shall be allowed as a depreciation deduction a reasonable allowance for the exhaustion, wear and tear (including a reasonable allowance for obsolescence)—
>
> (1) of property used in the trade or business, or
>
> (2) of property held for the production of income.
>
> . . . .

26 U.S.C. § 167(a) (1988).

The Treasury Regulation interpreting I.R.C. § 167(a) states in relevant part:

> If an intangible asset is known from experience or other factors to be of use in the business or in the production of income for only a limited period, the length of which can be estimated with reasonable accuracy, such an intangible asset may be the subject of a depreciation allowance. Examples are patents and copyrights. An intangible asset, the useful life of which is not limited, is not subject to the allowance merely because, in the unsupported opinion of the taxpayer, the intangible asset has a limited useful life. No deduction for depreciation is allowable with respect to goodwill.

Treas. Reg. § 1.167(a)-3 (1991).

STATEMENT OF THE CASE

This case presents a conflict among the circuits on a nationally-significant issue affecting billions of tax dollars. The issue concerns taxpayers' rights to depreciate intangible assets that are useful in their businesses for only a limited time. The court below held, as a matter of law, that customer relationships are nondepreciable "goodwill," even if they have determinable, limited durations and ascertainable values. (App. at 29a). That ruling calls into question the depreciability of over $10.5 billion of "customer/market-based intangible assets"; it affects the value of newspaper and magazine subscriptions, bank deposits, insurance relationships, and a host of other commercial and market relationships in seven major industry groups (manufacturing, finance/insurance/real estate, services, transportation, retail, wholesale trade, and mining). *See* United States General Accounting Office, *GAO/GCD-91-99 Tax Policy, Issues and Policy Proposals Regarding Tax Treatment of Intangible Assets* (Aug. 1991) [hereinafter "GAO Report"], at 4, 20, 22, 28-29. The ruling below is in direct, acknowledged conflict with decisions in two other circuits and the United States Tax Court, resulting in differing treatment of identically-situated taxpayers. Moreover, because there are far more numerous and fundamental decisional conflicts than the court of appeals acknowledged, the magnitude of the problem is even greater. A uniform rule of decision is critical.

A. Statement of Facts

Petitioner Newark Morning Ledger Co. ("Morning Ledger") is a newspaper publisher that is the successor to The Herald Company ("Herald"). In 1976, Herald purchased all of the stock of Booth Newspapers, Inc.

("Booth"), a publisher of daily and Sunday newspapers in eight Michigan communities. On May 31, 1977, Booth was merged into Herald. This transaction required Herald to allocate its adjusted tax basis in the Booth stock among the Booth assets in proportion to their fair market values as of the date of the merger.

As the Internal Revenue Service ("IRS") and Morning Ledger later stipulated, the total fair market value of the Booth assets on May 31, 1977, was approximately $314 million. (App. at 36a). Approximately $224 million of the total fair market value was allocated among various financial, tangible and other assets, and approximately $90 million was allocated to intangible assets. Of the $90 million allocated to intangible assets, approximately $67 million was allocated to the "paid subscribers" of the eight Booth newspapers (App. at 47a-48a), and $23 million was allocated to the going concern value and goodwill value of the newspapers. This dispute centers on whether the $67 million value of the "paid subscribers" was depreciable.

The "paid subscribers" are an example of an asset commonly known as a "customer-based" intangible asset. *GAO Report* at 20-22.[2] The "paid subscribers" were those individually identified customers who, under terminable-at-will contracts with the papers, contracted for delivery of a newspaper to a specific address on a regular basis in return for payment of the subscription price. These customers comprised a category distinct from the unknown customers—those who purchased their newspaper from a newsstand, a coin box, or other outlet—and from customers who purchased advertising.

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[2] *See also* H.R. Conf. Rep. No. 495, 100th Cong., 1st Sess. 936-37, *reprinted in* 1987 U.S.C.C.A.N. 2313-1245, 2313-1682-83; H.R. Rep. No. 391(II), 100th Cong., 1st Sess. 1058-59, *reprinted in* 1987 U.S.C.C.A.N. 2313-378, 2313-673-74.

Beginning in 1977, Herald claimed depreciation deductions with respect to the value of the paid subscribers. Herald did *not* claim depreciation deductions for any of the value of goodwill, which was comprised, *inter alia*, of the papers' name recognition, reputation, and relationships with non-subscription customers and customers who purchased advertising.[3] The IRS disallowed the claimed deductions, asserting that the paid subscribers were also part of the "goodwill" of the papers, and were therefore nondepreciable. Herald paid the additional taxes and interest, and Morning Ledger, as Herald's successor, filed a refund claim for the taxable years 1977 through 1980. When the IRS failed to act on the claim within the Code-prescribed period, Morning Ledger filed suit in the United States District Court for the District of New Jersey.

B. Proceedings Below

The case was tried to the district court on February 5 through February 8, 1990. From the outset, Morning Ledger and the government agreed that, under the widely followed two-pronged *Houston Chronicle* test,[4] in order to

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[3] In general, newspapers have two potential sources of revenue: paid circulation (*i.e.*, sales of the paper itself) and sales of advertising. Advertising sales account for either all (in the case of a free distribution paper) or the bulk (in the case of a paid circulation paper) of total revenue.

Approximately 80% of the total revenue of the Booth newspapers came from advertising sales. The remaining 20% of total revenue was made up of circulation revenue from the paid subscribers (approximately 85%) and circulation revenue from coin box, newsstand, and other sales. With respect to the non-subscription circulation revenue stream and the advertising sales revenue stream, since the "life" of a relationship with an unknown purchaser at a newsstand or coin box, or a particular advertiser, cannot be determined nor its value ascertained, the prospect for the continuation of such sales is goodwill and was, concededly, nondepreciable.

[4] *See Houston Chronicle Publishing Co. v. United States*, 481 F.2d 1240, 1249-50 (5th Cir. 1973), *cert. denied*, 414 U.S. 1129 (1974).

prevail Morning Ledger had to establish: (1) that the paid subscribers had limited useful lives, the duration of which could be estimated with reasonable accuracy; and (2) that the paid subscribers had an ascertainable value separate and distinct from goodwill. (App. at 32a).

Morning Ledger presented four witnesses, two of them experts, to prove that on May 31, 1977, the paid subscribers of the eight Booth newspapers had limited useful lives, the duration of which could be estimated with reasonable accuracy. The government offered no evidence to contest this testimony. Indeed, the government stipulated to the duration of the paid subscriber relationships in the event that the district court made certain predicate findings.[5] The district court made those findings, as well as the ultimate finding that Morning Ledger had proved that the paid subscribers had limited useful lives with determinable durations, satisfying the first prong of the two-part test for depreciability.[6]

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[5] Morning Ledger and the government stipulated to specific separate useful lives for both the daily subscriber relationships and the Sunday subscriber relationships for each of the eight Booth newspapers. The lives of these sixteen distinct subscriber relationships ranged from 14.7 to 23.4 years depending on the particular newspaper. (App. at 39a).

[6] Specifically, the district court stated:

> It is undisputed that all the paid subscribers of the Booth newspapers as of May 31, 1977 would, at some point in time, no longer be subscribers. . . . Subscribers are lost because of death, relocation, lack of reader time or interest, changing lifestyles, and other factors that are beyond the control of the newspapers. Also, subscribers are lost due to dissatisfaction with the product or service and for various other reasons, including competition from other media sources such as radio, television, magazines and other paid-circulation and/or free distribution newspapers.

(App. at 40a). The district court also found that the paid subscribers were not self-regenerating assets, meaning "there is no automatic replacement for a subscriber who terminates his or her subscription."

On the second inquiry—proof of an ascertainable value—Morning Ledger presented two additional expert witnesses who valued the paid subscribers. These experts utilized the "income method" of valuation. They calculated "the present value of the net revenue stream [the subscribers] would provide over their limited lives, i.e., the subscription revenue less the cost of collecting that revenue." (App. at 44a). The government asserted that the "cost method" was the only proper valuation technique. However, Morning Ledger's experts testified that use of the cost method was inappropriate in this case. The district court rejected the government's contention and found that the government's experts "were unqualified, valued the wrong asset [a customer list as opposed to the paid subscribers] and utilized inappropriate methodology." (App. at 43a).[7]

(App. at 40a). These facts distinguished the paid subscribers from goodwill, which "by definition, has an indefinite life . . . ." (App. at 45a).

[7] The fair market value of an asset is the price at which the asset would change hands between a hypothetical willing buyer and willing seller, neither being under any compulsion to buy or sell, and both parties having reasonable knowledge of the relevant facts. Three valuation techniques are generally used to determine fair market value: (1) the market method, (2) the cost method, and (3) the income method.

In this case, the data was not sufficient to utilize the market method, which requires a sufficient number of actual transactions in the asset to be valued. (App. at 42a). The income method that Morning Ledger's experts employed is, the district court found, "commonly used to value intangible assets of a going business, other than goodwill and going concern value." (App. at 43a). The district court also found that the income method "is, in fact, what buyers and sellers would utilize to determine the price at which these assets would change hands." (App. at 43a). The government's cost method essentially measured only the direct cost of compiling a list of names (*i.e.*, a customer list); it did not measure the value of the subscriber relationships. Morning Ledger's experts testified that the cost method accordingly was inappropriate, and the district court found the cost method "could not and should not be used to determine the fair market value of the paid subscribers of the Booth newspapers as of May 31, 1977." (App. at 43a). Because the government's method "totally ignore[d]" Morning Ledger's "sub-

Furthermore, the government "refused to provide contradictory expert valuation under the income method." (App. at 7a n.2). Accordingly, finding that the government "offered no competent evidence to the court upon which the court could base any finding to reduce [Morning Ledger's] evidence of valuation," and that Morning Ledger's methodology "was fully in accordance with generally accepted valuation principles," the district court adopted Morning Ledger's methodology and the $67 million valuation of the paid subscribers. (App. at 44a-45a).

The district court also found that the paid subscribers were intangible assets separate and distinct from goodwill:

> [P]aid subscribers are distinct from previous customers who may or may not return, who may buy more or less or nothing at all. They are identifiable; how long they will remain as subscribers can be predicted with reasonable accuracy; and their value can be measured with a fair degree of accuracy. It is these unique characteristics which separates them from general goodwill and permits of a separate valuation.

(App. at 45a). As the district court held, the differentiation between nondepreciable goodwill and the depreciable, customer-based intangible asset at issue here turned on a distinction between "a galaxy of customers who may or may not return, whose frequency is unknown, and whose quantity of future purchases cannot be predicted" and, in contrast, "subscribers who can be predicted to purchase the same item, for the same price on a daily basis." (App.

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stantial efforts and expenses . . . invested over the years in establishing those subscriber relationships" (App. at 43a), it undervalued the paid subscribers, and hence could not yield their fair market value. (App. at 43a-44a).

at 32a-33a).[8] The $67 million value allocated to the latter (the paid subscribers), was separate and distinct from the $23 million allocated to the former (goodwill and going concern value). Morning Ledger was, therefore, entitled to depreciate the value of the paid subscribers.

On September 12, 1991, the Third Circuit reversed. It held that the paid subscribers were not depreciable, notwithstanding the district court's findings that the paid subscribers had limited useful lives and an ascertainable value, making them separate and distinct from goodwill. Instead, seizing upon the notion that any asset that contributes to continued patronage is "inherently" goodwill, the Third Circuit found that certain customer-based intangible assets, including the paid subscribers here, are nondepreciable goodwill as a matter of law. Nevertheless, the Third Circuit suggested that had Morning Ledger valued the paid subscribers pursuant to the cost method, and not the income method, the paid subscribers somehow may have been transformed from nondepreciable goodwill into depreciable intangible assets.

In holding that the paid subscription relationships were not depreciable, the Third Circuit placed considerable emphasis on the fact that the subscriptions were not formally embodied in fixed-term contracts. The Third Circuit held that contractually-based patronage was not "goodwill," and observed that "if the subscribers were contractually obligated to continue subscribing for some period of time, Morning Ledger *clearly* would be permitted to depreciate the value of those contracts over that time period." (App.

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[8] Morning Ledger's evidence also established that in the newspaper business, goodwill and paid subscribers often exist separately. For example, a profitable free-distribution newspaper would have goodwill, but does not have any paid subscribers. Its goodwill is derived from advertisers, name recognition, place of distribution, and the like. Conversely, a newspaper could have paid subscribers but lack goodwill if it were bankrupt or unprofitable.

at 11a-12a) (emphasis added). The court distinguished Morning Ledger's paid subscribers on grounds that those relationships were terminable-at-will contracts. (App. at 12a). It did not explain, in a case where Morning Ledger had proved that the life of the relationships was limited, and the parties had stipulated their duration (factual findings left undisturbed), why there was a difference, for purposes of depreciability, between fixed-term contracts and terminable-at-will contracts with ascertainable lengths.

On October 15, 1991, the Third Circuit denied Morning Ledger's petition for rehearing and suggestion for rehearing *en banc*. Two Circuit Judges, Greenberg and Nygaard, dissented.

REASONS FOR GRANTING THE PETITION

This case merits review because the Third Circuit, in acknowledged and direct conflict with other circuit courts and the Tax Court, has adopted a rule of law that transforms a large class of wasting intangible assets into nondepreciable "goodwill." The assets, worth billions of dollars, were heretofore widely held depreciable. Accordingly, this new legal rule produces differing tax treatment of identically-situated taxpayers.

The writ should be granted for three reasons. *First*, the Third Circuit's decision has resulted in a split among the circuit courts concerning the basic test for determining whether an intangible asset is depreciable or is instead nondepreciable goodwill. It has also created a direct and acknowledged split in the circuits on the depreciability of the customer-based intangible assets at issue in this case. As a result, there is uncertainty as to whether a host of intangible assets, long-recognized to be depreciable, are

now *per se* nondepreciable goodwill, despite the taxpayer's ability to prove that they are truly wasting assets.[9]

Second, the Third Circuit's error is a matter of substantial national significance. A nationwide General Accounting Office study indicates that as of 1989, in audited matters alone, taxpayers across the country had claimed depreciation deductions for $10.5 billion in customer-based and market-based intangible assets, and that the IRS had proposed adjustments in hundreds of such cases, aggregating over $4 billion in taxes. *GAO Report* at 22. If left unreviewed, the conflicts resulting from the Third Circuit's decision infect these cases and countless other transactions involving billions of dollars with uncertainty. If left unresolved, the conflicts ensure differential treatment of taxpayers from circuit to circuit, with enormous financial and legal consequences. It is crucial for the proper and consistent administration of the nation's revenue laws that this Court grant the petition and review the judgment below.

Third, in radically expanding the concept of goodwill to bar the depreciation of certain wasting assets, the Third Circuit has contravened the basic tax principle embodied in Section 167 of the Internal Revenue Code and the interpreting regulation that wasting assets *shall* be depreciable. Goodwill has long been held to be nondepreciable precisely because it is *not* a wasting asset—that is, it has an indefinite life. The Third Circuit's decision abandons this principle by radically expanding the concept of non-

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[9] It is well-established that uniformity among the circuits in tax cases is especially important in order to ensure predictable and equal administration of the federal income tax system. *See, e.g., United States v. Gilbert Assocs., Inc.*, 345 U.S. 361, 364 (1953); *Unger v. Commissioner*, 936 F.2d 1316, 1320 (D.C. Cir. 1991); *Nickell v. Commissioner*, 831 F.2d 1265, 1270 (6th Cir. 1987); *First Charter Fin. Corp. v. United States*, 669 F.2d 1342, 1345 (9th Cir. 1982).

depreciable "goodwill" to include intangible assets "notwithstanding that they have wasting lives." (App. at 29a).[10]

I.

CERTIORARI SHOULD BE GRANTED TO RESOLVE THE CONFLICT AMONG THE CIRCUITS REGARDING THE STANDARD FOR DEPRECIABILITY OF INTANGIBLE ASSETS UNDER THE INCOME TAX LAWS.

Section 167(a) of the Internal Revenue Code allows as a depreciation deduction a reasonable allowance for the exhaustion, wear and tear, and obsolescence of property, both tangible and intangible, used in a trade or business. Treasury Regulation 1.167(a)-3 identifies the circumstances under which an intangible asset may be depreciated:

> If an intangible asset is known from experience or other factors to be of use in the business or in the production of income for only a limited

[10] Moreover, not since the days of Prohibition has this Court addressed the issue of goodwill under the nation's revenue laws. *See Gambrinus Brewery Co. v. Anderson*, 282 U.S. 638, 641-44 (1931); *Clarke v. Haberle Brewing Co.*, 280 U.S. 384, 386-87 (1930). Not surprisingly, the longstanding confusion concerning the relationship between the depreciation of intangible assets and nondepreciable goodwill under the Internal Revenue Code has produced considerable commentary. *See, e.g.*, Danny P. Hollingsworth and Walter T. Harrison, *Taxation of Intangibles*, 9 J.L. & Com. 51 (1989); George Mundstock, *Taxation of Business Intangible Capital*, 135 U. Pa. L. Rev. 1179 (1987); Lawrence M. Dubin, *Allocation of Costs to, and Amortization of, Intangibles in Business Acquisitions*, 57 Taxes 930 (1979); Martin J. Gregorcich, *Amortization of Intangibles: A Reassessment of the Tax Treatment of Purchased Goodwill*, 28 Tax Law. 251 (1975); Note, *Amortization of Intangibles: An Examination of the Tax Treatment of Purchased Goodwill*, 81 Harv. L. Rev. 859 (1968); Alan S. Schenk, *Depreciation of Intangible Assets: The Uncertainty of Death and Taxes*, 13 Wayne L. Rev. 501 (1967); Robert J. McDonald, *Goodwill and the Federal Income Tax*, 45 Va. L. Rev. 645 (1959); Note, *An Inquiry Into the Nature of Goodwill*, 53 Colum. L. Rev. 660 (1953); Floyd A. Wright, *The Nature and Basis of Legal Goodwill*, 24 Ill. L. Rev. 20 (1929).

> period, the length of which can be estimated with reasonable accuracy, such an intangible asset may be the subject of a depreciation allowance. Examples are copyrights and patents.

Because it is universally accepted that goodwill is not "of use . . . for only a limited period," but instead has an indefinite life,[11] Treasury Regulation 1.167(a)-3 also provides that goodwill is not depreciable.

Prior to the Third Circuit's decision, it was uniformly recognized that whether a particular intangible asset is depreciable under Section 167(a) of the Internal Revenue Code turned on whether the taxpayer can establish that the asset has an ascertainable value separate and distinct from goodwill; and has a limited useful life, the duration of which can be ascertained with reasonable accuracy. *See generally Houston Chronicle*, 481 F.2d at 1248-50.[12] As applied, this test was consistently construed to allow the depreciation of *any* intangible asset that was demonstrated to have a wasting life with ascertainable value.

This case squarely presents a split in the circuits, for the Third Circuit has now rejected this approach. Instead, the Third Circuit has held that certain classes of intangible assets are nondepreciable as a matter of law, *notwith-*

[11] *See, e.g., Patterson v. Commissioner*, 810 F.2d 562, 569 (6th Cir. 1987) (goodwill "does not waste"); *Houston Chronicle*, 481 F.2d at 1248, (goodwill is "an ongoing asset that fluctuates but does not necessarily diminish"); *Colorado National Bankshares, Inc. v. Commissioner*, 60 T.C.M. (CCH) 771, 789 (1990) ("Goodwill, by definition, has an indefinite life . . . ."); *Computing & Software, Inc. v. Commissioner*, 64 T.C. 223, 233 (1975), *acq.*, 65 T.C. 1153 (1976) (goodwill "may be expected to continue indefinitely").

[12] Indeed, in this very case, the government stipulated that this factual test was the proper method to determine whether an intangible asset is subject to a depreciation allowance. It was only *after* the district court made factual findings in favor of the petitioner that the government sought to argue that the issue of depreciability was a question of law.

standing proof and a determination by the factfinder that the particular asset at issue meets the requirements for depreciability under the *Houston Chronicle* test. Review by this Court is necessary to resolve this conflict among the circuits.

Seizing upon the oft-quoted but highly amorphous notion that goodwill is "the expectancy that old customers will resort to the old place," the Third Circuit made the sweeping conclusion that certain customer-based intangible assets transferred as part of a going concern are "inherently" goodwill because they contribute to continued patronage. Thus, despite the district court's finding that the value assigned to the particular customer-based assets depreciated in this case *was* separate and distinct from the newspapers' $23 million goodwill value (which was tied to, *inter alia*, *non*-subscription customers and advertisers), the Third Circuit held that the assets were *per se* nondepreciable.

The Third Circuit's decision that certain customer-based intangible assets transferred as part of a going concern are nondepreciable as a matter of law is in direct conflict with decisions by the Seventh, Eighth, Ninth, Eleventh and Federal Circuits, as well as the full panel of the Tax Court.[13] These courts have all explicitly held that customer-based intangible assets transferred as part of a going concern are depreciable pursuant to Section 167(a) of the Internal Revenue Code if, as with all types of intangible assets, the taxpayer demonstrates that the asset has an ascertainable value and a limited useful life. The Third Circuit's decision cannot be reconciled with these decisions.

[13] *See Donrey, Inc. v. United States*, 809 F.2d 534 (8th Cir. 1987); *Richard S. Miller & Sons, Inc. v. United States*, 537 F.2d 446 (Ct. Cl. 1976); *Super Food Services, Inc. v. United States*, 416 F.2d 1236 (7th Cir. 1969); *Commissioner v. Seaboard Finance Co.*, 367 F.2d 646 (9th Cir. 1966); *Citizens & Southern Corp. v. Commissioner*, 91 T.C. 463 (1988), *aff'd*, 919 F.2d 1492 (11th Cir. 1990); *see also IT&S of Iowa, Inc. v. Commissioner*, 97 T.C. ___, [Current Regular Dec.] Tax Ct. Rep. (CCH) No. 34 (Nov. 12, 1991); *Colorado National*, 60 T.C.M. (CCH) 771 (1990); *Los Angeles Cent. Animal Hosp., Inc. v. Commissioner*, 68 T.C. 269 (1977), *acq.* 1978-2 C.B.2, *acq.* 1978-1 C.B.2; *First Pennsylvania Banking & Trust Co. v. Commissioner*, 56 T.C. 677 (1971), *acq.* 1972-1 C.B. 2.

For example, in *Donrey*, a case the Third Circuit acknowledged was "undeniably similar" (App. at 18a), the taxpayer purchased an Indiana newspaper that had approximately 11,000 paid subscribers. From the $1.3 million purchase price, the taxpayer allocated about half—approximately $560,000—to the subscription structure and sought to depreciate that amount. The government argued, as it did here, that the paid subscriber relationships represented continued patronage and were thus goodwill; but the jury found that Donrey had proved limited useful lives for its subscriber structure and a value ($560,000) that was separate and distinct from goodwill ($122,000). *Donrey*, 809 F.2d at 535-36. The Eighth Circuit affirmed the depreciability of the subscribers, rejecting the government's contention that the subscription structure was part of nondepreciable goodwill as a matter of law. *Id.* at 536.

The Third Circuit has now adopted the very argument the *Donrey* court rejected.[14] Morning Ledger proved limited useful lives for its paid subscribers, and the district court found a value for the subscription structures ($67 million) that was separate from the value of goodwill and going concern ($23 million). (App. at 5a, 7a, 47a). Such

[14] The Third Circuit did so in part on the mistaken belief that "[i]t would appear that *Houston Chronicle* and *Donrey* are directly in conflict." (App. at 19a). There is no such conflict. The district court judgment in *Donrey* was entered on the basis of jury interrogatories that tracked the *Houston Chronicle* standard, and the Eighth Circuit expressly cited *Houston Chronicle* with approval when it affirmed that judgment. *See Donrey*, 809 F.2d at 536-37. No other court has suggested these two decisions conflict in any way. To the contrary, the Tax Court recently cited both cases as standing for the same proposition. *IT&S of Iowa*, 97 T.C. ___, [Current Regular Dec.] Tax Ct. Rep. (CCH) at 4555-56.

proof of a limited life and a separate value rendered the subscriber-based asset depreciable in *Donrey*, *see* 809 F.2d at 536, but the Third Circuit nevertheless held that newspaper paid subscribers (and other similar intangible assets) were nondepreciable goodwill.

Similarly, the Third Circuit "respectfully disagree[d]" with the Eleventh Circuit's affirmance of the full Tax Court's decision in *Citizens & Southern*. (App. at 22a n.7a). In *Citizens & Southern*, the taxpayer acquired nine banks, allocating $10.4 million of the total purchase price to goodwill and $41.7 million to customer-based intangible assets denominated "deposit base." These "core deposits" were customer relationships indistinguishable from newspaper paid subscriber relationships. They were comprised of and valued on the future income stream (patronage) resulting from certain terminable-at-will checking and savings accounts existing at the time of acquisition. The IRS disallowed depreciation of the core deposits on "the assumption that terminable-at-will relationships represent goodwill." *Citizens & Southern*, 91 T.C. at 483. Yet, after an exhaustive review of the authorities, the full Tax Court rejected the government's argument. *Id.* at 483-90. The Eleventh Circuit affirmed the holding that the core deposit accounts were a depreciable intangible asset based on the Tax Court's opinion, *see* 919 F.2d at 1492, a result that cannot be squared with the result below.[15]

[15] The Third Circuit also admitted the "analytic force" of *Colorado National*, another Tax Court decision holding that core deposits could be depreciated, but chose not to follow it. (App. at 28a). In *Colorado National*, a taxpayer that acquired seven banks for a total purchase price of $88.2 million allocated $41.4 million to core deposits and $5.7 million to goodwill. 60 T.C.M. (CCH) at 776-77. The Tax Court held that terminable-at-will core deposits could be depreciated, because this customer-based intangible asset, while "closely interrelated to goodwill, . . . is nevertheless a separate and distinct asset," and it explicitly rejected the government's invitation to "inquire into the intrinsic nature of the asset measured and determine whether it is, in essence, goodwill." 60 T.C.M. (CCH) at 789-90. The Third Circuit recognized that *Colorado National* held "that any intangible asset possessing a determinable life and an ascertainable value is, by definition, not goodwill." (App. at 22a). Yet the Third Circuit then held exactly the opposite, with its assertion that "some" wasting intangible assets "are nonetheless goodwill." (App. at 29a).

Most recently, in *IT&S of Iowa*, a decision handed down subsequent to the Third Circuit's opinion, the government again asserted that the net income stream attributable to terminable-at-will core deposit accounts was future patronage/goodwill, representing no more than "inertia" where customers "[left] funds on deposit for an ascertainable length of time." 97 T.C. ___, [Current Regular Dec.] Tax Ct. Rep. (CCH) at 4556. The Tax Court reaffirmed *Citizens & Southern* and rejected this argument, holding that even though "a deposit account has no fixed termination date and is terminable at will," a taxpayer could prove the core deposits were an intangible asset separate and distinct from goodwill. *Id.* The ruling below is exactly the opposite.

For purposes of determining whether a customer-based asset is depreciable, the Third Circuit drew a decisionally-decisive distinction between fixed-term and terminable-at-will customer relationships. No other court has adopted this arbitrary distinction. Indeed, other courts have rejected it, creating a clear conflict. In *Super Food Services*, the taxpayer acquired a number of franchise contracts that were terminable-at-will on 30 days notice. However, the taxpayer offered proof that these terminable-at-will relationships had an average life of seven years. Rejecting the government's attempt to draw a distinction based on the form, rather than the substance, of the relationship, the Seventh Circuit held "it is immaterial that the contracts may have no fixed termination date" and "it also is immaterial whether these [at-will] contracts were acquired separately or as part of a going business." 416 F.2d at 1240. *See also Citizens & Southern*, 91 T.C. at 486 ("The fact that a deposit account has no fixed termination date and is terminable at will does not as a matter of law prevent [the taxpayer] from showing that [the asset] has an ascertainable cost basis separate and distinct from goodwill and that it has a reasonably ascertainable useful

life."); *accord IT&S of Iowa*, 97 T.C. ___, [Current Regular Dec.] Tax Ct. Rep. (CCH) at 4556 (even though "a deposit account has no fixed termination date and is terminable at will," a taxpayer can prove that the intangible asset is separate and distinct from goodwill).

The district court in this case had the proper analysis. Unlike the court of appeals, it recognized that the proper distinction was not one of form—between fixed-term and terminable-at-will relationships—but rather one of substance—between those relationships that are immeasurable and indefinite (goodwill) and those that have *determinable* lives and values:

> [O]ne must distinguish between a galaxy of customers who may or may not return, whose frequency is unknown, and whose quantity and future purchases cannot be predicted, against subscribers who can be predicted to purchase the same item, for the same price on a daily basis. . . . [T]he income derived from such paying subscribers will recur, which, in turn, permits the ascertainment of value separate and apart from goodwill.

(App. at 33a.)

In essence, the Third Circuit has transformed the vague *concept* of "goodwill" into the *test* for determining whether intangible assets are depreciable under Section 167(a) of the Internal Revenue Code. Contrary to the Third Circuit's decision, the oft-quoted description of goodwill—"old customers will resort to the old place"—was never intended, and has never before been invoked, as a dispositive litmus test that bars the depreciation of truly wasting intangible assets. To the contrary, in recognition that intangible assets may contribute to continued patronage yet still have "value separate and distinct from goodwill," courts have uniformly allowed depreciation deductions under Section 167(a) for a host of intangible assets that contribute to

continued patronage, including customer-based intangible assets (without fixed-term contracts) transferred as part of a going concern.[16]

In effect, the Third Circuit has significantly modified the widely-accepted *Houston Chronicle* test to require a three-part showing that the asset (i) has a limited useful life; (ii) has an ascertainable value; *and* (iii) has *no* indicia of goodwill whatsoever. In contrast, as applied by other courts, the *Houston Chronicle* test only requires proof that the asset is wasting (*i.e.*, requirement (i)) and that the ascertainable *value* for which a depreciation deduction is sought is separate and distinct from goodwill. In short, there simply is "no authority for the proposition that assets, intangible or tangible, are not separate and distinct from goodwill unless no part of their value is related to continued patronage of customers of an ongoing business." *Citizens & Southern*, 91 T.C. at 515 (Cohen, J., concurring); *accord Seaboard Finance*, 367 F.2d at 651.

As a result of the Third Circuit's decision, a host of intangible assets, long-recognized to be depreciable under Section 167(a) of the Internal Revenue Code because of their wasting nature, are now at risk of being labelled *per se* nondepreciable goodwill merely because they contribute to continued patronage. For example, if followed consistently, the Third Circuit's litmus test approach to goodwill would render a patent—explicitly recognized under Treasury Regulation 1.167(a)-3 as a depreciable intangible asset because of its limited useful life—nondepreciable "good-

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[16] Moreover, many courts that found customer-based intangible assets depreciable also recognized that goodwill is the concept that "old customers will resort to the old place" or is related to "continued patronage." *See, e.g., Richard S. Miller & Sons*, 537 F.2d at 450; *Seaboard Finance*, 367 F.2d at 649; *Citizens & Southern*, 91 T.C. at 480; *Colorado National*, 60 T.C.M. (CCH) at 787; *Los Angeles Cent. Animal Hosp.*, 68 T.C. at 273. Thus, the Third Circuit's assertion that courts which found customer-based intangible assets depreciable had applied the wrong "definition" of goodwill (App. at 23a) was plainly wrong.

will" if it contributes in any way to "the expectancy that old customers will resort to the old place." *Cf. Richard S. Miller & Sons*, 537 F.2d at 450. Similarly, fixed-term customer contracts undeniably contribute to future patronage, yet the Third Circuit conceded that such assets are depreciable pursuant to Section 167(a). (App. at 11a-12a).

The Third Circuit erroneously held that certain customer-based intangible assets transferred as part of a going concern are *per se* nondepreciable goodwill, and thus did not have to decide what valuation method was appropriate in this case. Nevertheless, it curiously went on to suggest that, had the taxpayer in this case valued the intangible assets pursuant to the cost method (*i.e.*, the cost of generating subscribers), rather than the income method (*i.e.*, the stream of income to be generated by the subscribers over their remaining useful lives), the assets would have been transformed from nondepreciable goodwill into depreciable intangible assets. The Third Circuit's apparent insistence on the use of the cost method conflicts with the decisions of every other court to consider the issue of depreciability under I.R.C. § 167(a).

Where taxpayers have sought to establish the value of a wasting intangible asset pursuant to the income method, courts have consistently allowed such valuations.[17] Indeed, intangible assets are *normally* valued pursuant to the income method under the tax laws, for this is the method a willing buyer and willing seller would ordinarily apply in determining the asset's sales price. (App. at 43a-44a); *see Colorado National*, 60 T.C.M. (CCH) at 792. *See generally United States* v. *Ludey*, 274 U.S. 295, 301 (1927); *supra* p. 7 n.7. Petitioner has been unable to find any decision, other than the Third Circuit's decision in this

[17] *See Citizens & Southern*, 91 T.C. at 505-06; *Colorado National*, 60 T.C.M. (CCH) at 792-94; *First Pennsylvania*, 56 T.C. at 692-97; *see also* App. at 18a (noting use of income method in *Donrey*).

case, that suggests that an intangible asset cannot be depreciated (*i.e.*, it is not a wasting asset) if valued pursuant to the income method.

II.

CERTIORARI SHOULD BE GRANTED TO RESOLVE A RECURRING DISPUTE OF ENORMOUS CONSEQUENCE CONCERNING THE ADMINISTRATION OF THE INCOME TAX LAWS.

The decision below has ramifications far beyond the instant case. The decade of the 1980s saw more than 31,000 reported business merger, acquisition, and divestiture transactions, with an aggregate value of more than $1.3 trillion. Martin Sikora, *The M&A Bonanza of the '80s . . . And Its Legacy*, Mergers & Acquisitions, Mar.-Apr. 1990, at 90.

In August 1991, the GAO prepared and issued a report to the Joint Congressional Committee on Taxation analyzing how the purchase price for acquired businesses was allocated among intangible assets. The GAO examined tax data the IRS had gathered in 1989 (generally covering tax years 1979 to 1987) from the IRS's unresolved, or open, purchased intangible asset cases. *GAO Report* at 13. It is important to note that the data the GAO examined reflects only a small portion of the purchased intangible asset universe: the data did not include unaudited tax returns, cases that had been closed, and post-1987 matters. *Id.*

Based on this data, the GAO estimated that from 1979 to 1987, taxpayers in nine major industry groups had claimed deductions for 175 types of purchased intangible assets, identified as distinct from goodwill, and valued at $23.5 billion. *GAO Report* at 3. By far the "largest category of intangibles" was the "customer- or market-based assets," assets that "related to the customer structure or market factors of a business." *Id.* at 22. Among the examples, the GAO listed core deposits, customer relations,

customer structure, and subscription lists. *See id.* at 40-42. Taxpayers in seven of the nine major industry groups had allocated $10.5 billion to these customer/market-based intangible assets, nearly three times the amount allocated to the next largest intangible category. *Id.* at 22. None of these assets were embodied in fixed-term contracts; the GAO separately reported what it called "contract-based intangible assets." *Id.* at 22.

As of 1989, the IRS identified 776 open audit matters involving these customer/market-based intangibles in its examination, appeals, and litigation units. *Id.* at 4, 22. The IRS had proposed tax adjustments of over $4.1 billion in these 776 cases, more than half of the total adjustments for *all* intangibles. *Id.* Indeed, as a general matter, the GAO found that "[i]n 70 percent of the cases in which taxpayers claimed that intangible assets had a determinable useful life, IRS claimed that the assets were in fact goodwill and not amortizable." *Id.* at 4.

Because of the overwhelming recurrence of the disputed issue here and its enormous consequence in the administration of the nation's revenue laws, review by this Court is imperative. *See, e.g., Commissioner v. Glenshaw Glass Co.*, 348 U.S. 426, 427 (1955).

III.

CERTIORARI SHOULD BE GRANTED BECAUSE THE THIRD CIRCUIT'S DECISION IS A SERIOUS DEPARTURE FROM THE GOVERNING STATUTE.

The Third Circuit's decision that certain customer-based assets are *per se* nondepreciable goodwill is flatly inconsistent with Section 167(a) of the Internal Revenue Code. Fundamentally, income tax is a tax on *net* income. To enable a business to offset annual expenses against revenues, Congress has specifically authorized depreciation deductions for wasting assets. *See Gambrinus Brewery Co.*, 282 U.S. at 643. For if a taxpayer cannot depreciate the

value of a wasting asset but is still taxed on the income the asset produces, the taxpayer would be taxed on more than the *net* income the taxpayer has actually earned. Section 167(a) of the Code, which embodies this principle, thus provides that a depreciation deduction "shall be allowed" for the "exhaustion" of property used in a business or to produce income.

To effect the statute's purpose, courts have always treated intangible assets with identifiable limited useful lives like tangible property for purposes of depreciation. *See Richard S. Miller & Sons*, 537 F.2d at 450. Thus, customer-based intangible assets with proven limited lives have consistently been found to be depreciable. *See, e.g., Super Food Services*, 416 F.2d at 1240; *Citizens & Southern*, 91 T.C. at 480-89 (collecting cases). Morning Ledger's paid subscriber relationships were intangible assets (property) that, under the district court's findings, were being exhausted (*i.e.*, they had wasting lives). A depreciation deduction would have been available, but for the Third Circuit's unprecedented inclusion of assets with definite and wasting lives in "goodwill."

There is simply no authority to suggest that Congress intended to limit depreciation deductions to assets that have no connection whatsoever to future patronage. Rather, the deductions are intended to match actual expense against income. To achieve this end, a depreciation deduction must apply to all wasting assets. The *Houston Chronicle* court put the point well. Referring to the Eighth Circuit's decision in *Northern Natural Gas Co. v. O'Malley*, 277 F.2d 128 (8th Cir. 1960), the court stated:

> As the concurring opinion of then-Circuit Judge Blackmun makes clear, if the asset is shown to be a wasting one used in the taxpayer's trade or business, a reasonable deduction *must* be allowed.

Houston Chronicle, 481 F.2d at 1251 (emphasis added).[18]

[18] The majority view—that customer-based intangible assets are de-

Accordingly, the applicable Treasury regulation states that an intangible asset known to be of use "for only a limited period" may be "the subject of a depreciation allowance." Treas. Reg. § 1. 167(a)-3. Limited life is the crucial concept. The regulation continues that depreciation is *not* allowed for "[a]n intangible asset, the useful life of which is not limited . . . ." *Id.*

The reason goodwill is not depreciable under the Treasury regulation is precisely because goodwill is *not* a wasting asset—it does *not* have a definite life. The Third Circuit's ruling discards this universally-accepted, fundamental characteristic of goodwill—a characteristic that served not only to define but, just as importantly, to limit the parameters of "goodwill." The focus on a determinable, limited life in the Internal Revenue Code and Treasury regulation enables questions of depreciability to be resolved without having to decide what "goodwill" is; it is enough if one knows what "goodwill" is not.

Thus, until the ruling below, courts consistently held that goodwill had an indefinite life. *See, e.g., Patterson*, 810 F.2d at 569 (goodwill "does not waste"); *Richard S. Miller & Sons*, 537 F.2d at 454 ("An intangible asset is separate and distinct from goodwill when its useful life can be shown with reasonable accuracy to be of limited duration."); *Houston Chronicle*, 481 F.2d at 1248 (goodwill is "an ongoing asset that fluctuates but does not necessarily diminish"); *Computing & Software*, 64 T.C. at 233 (goodwill "may be expected to continue indefinitely"); *Colorado National*, 60 T.C.M. (CCH) at 789 ("Goodwill, by

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preciable—is also consistent with generally accepted accounting principles, principles adopted by the Securities and Exchange Commission and other recognized practices in the business community relating to the identification of goodwill. *See, e.g., Colorado National*, 60 T.C.M. (CCH) at 788-89; *cf. Northern Natural Gas Co.*, 277 F.2d at 140 (Blackmun, J., concurring) (depreciation deduction for truly wasting asset "seems to me to coincide with good business practice and good accounting.")

definition, has an indefinite life . . . ."); *IT&S of Iowa*, 97 T.C. ___, [Current Regular Dec.] Tax Ct. Rep. (CCH) at 4556 ("mere inertia, which lasts for only a limited time, should not be equated with the continued patronage of a business over an indefinite period.").

The Third Circuit has now departed from this authority with its holding that "some intangible assets" are goodwill "notwithstanding that they have wasting lives that can be estimated with reasonable accuracy and ascertainable values." (App. at 29a). Until now, because a necessary characteristic of goodwill was an indefinite life, it was logically inescapable that the value of a wasting asset was not part of goodwill. Every court that had considered that issue had so held. *See Super Food Services*, 416 F.2d at 1240 (summary judgment for government improper where terminable-at-will franchise contracts had limited useful lives); *First Pennsylvania*, 56 T.C. at 697-98 n.12, (terminable-at-will customer contracts having a "definite life expectancy" may be valued separately from goodwill); *see also Richard S. Miller & Sons*, 537 F.2d at 452; *Seaboard Finance*, 367 F.2d at 653; *Colorado National*, 60 T.C.M. (CCH) at 790. The ruling below illogically results in assets with proven definite lives being treated as if they had indefinite lives. The Third Circuit's approach abandons a crucial and easily administered limitation on "goodwill" for a standardless inquiry into the "essence" of goodwill. A host of limited-life intangible assets are now at risk of being brought within some "penumbra" of "goodwill," and rendered nondepreciable, if they have *some* connection with patronage.

What the Third Circuit ignored is that implicit in the notion of goodwill is uncertainty. However, as the district court correctly found, there is no uncertainty associated with the paid subscribers at issue in this case. Their value "does not depend on some vague hope" that they will continue to purchase newspapers. *See Citizens & Southern*, 91 T.C. at 499; *Colorado National*, 60 T.C.M. (CCH) at

789. The value of the paid subscriber relationships here (like the customer relationships in *Citizens & Southern* and *Colorado National*) lies in the ascertainable probability, proved at trial and found by the district court, that these paid subscriber relationships will continue for predictable periods. The papers' goodwill, in contrast, is tied to *other* customers, such as advertisers or people who buy their papers at newsstands, who must make affirmative decisions to continue patronizing the newspaper. *Their* value and life are uncertain and, tellingly, no depreciation deduction was sought by Morning Ledger for those customer relationships.

CONCLUSION

The decision of the Third Circuit creates a square and acknowledged conflict in the circuits, drastically expands the concept of nondepreciable "goodwill," adopts a rule of law that is without basis in statutory or regulatory text, and affects billions of tax dollars. The decision creates inconsistency and uncertainty in the application of federal tax law to innumerable business transactions. Accordingly, this case presents a nationally-significant question of federal law that merits this Court's attention.

For the foregoing reasons, the petition for a writ of certiorari should be granted.

Respectfully submitted,

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January 13, 1992

APPENDIX

APPENDIX A

UNITED STATES COURT OF APPEALS
FOR THE THIRD CIRCUIT

NO. 90-5637

NEWARK MORNING LEDGER CO.,
AS SUCCESSOR TO THE HERALD COMPANY,
Appellee

v.

THE UNITED STATES OF AMERICA,
Appellant

On Appeal From The United States District Court
For The District of New Jersey
(D.C. Civ. No. 88-04836)

Argued: January 23, 1991

Decided: September 12, 1991

Before: BECKER and HUTCHINSON,
***Circuit Judges,* and SMITH,**
District Judge.*

As Amended on Denial of Rehearing October 15, 1991

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* Honorable D. Brooks Smith, United States District Judge for the Western District of Pennsylvania, sitting by designation.

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OPINION OF THE COURT

BECKER, Circuit Judge.

This appeal by the United States from an adverse judgment of the district court in a tax refund case raises important questions concerning a taxpayer's ability to depreciate acquired intangible assets. Taxpayer/appellee Newark Morning Ledger Co. ("Morning Ledger") acquired a corporation, which itself had previously acquired the assets of eight Michigan newspapers by means of an I.R.C. §§ 332, 334(b)(2) liquidation, and which had attempted to depreciate some $67 million of the purchase price as allocated to a category denominated "paid subscribers." This amount reflected an estimate by financial and statistical experts of the present value of the future profits to be derived from the 460,000 at-will subscribers acquired in the liquidation. The Internal Revenue Service ("the Service") disallowed the depreciation deductions on the ground that Morning Ledger's predecessor could not, by sophisticated and accurate expert analysis, convert into a depreciable asset what was quintessentially goodwill—i.e., the value of the expectation of continued patronage. The tax was paid, the refund suit ensued, and, after a bench trial, the district court entered judgment for Morning Ledger. For the reasons that follow, we will reverse.

I. FACTS AND PROCEDURAL HISTORY

Over a period of several months in 1976, the Herald Company ("Herald") purchased, through private sales and a public tender offer, all the outstanding stock of Booth Newspapers, Inc. ("Booth"), a Michigan corporation which published daily and Sunday newspapers in eight Michigan communities with a total at-will subscription of approximately 460,000.[1] In 1977, Herald liquidated the Booth

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[1] The eight Michigan newspapers published by Booth were the *Ann Arbor News; Bay City Times; Flint Journal; Grand Rapids Press;*

stock, received all the latter's assets, and continued publishing the eight newspapers under the same names. In 1987, Herald was merged into appellee Morning Ledger, a New Jersey corporation, effectively making the operations of Herald and Booth unincorporated divisions of Morning Ledger.

Herald's 1977 liquidation of the stock of Booth was carried out pursuant to sections 332 and 334(b)(2) of the Internal Revenue Code. These sections required Herald's $328,173,154 adjusted tax basis in Booth's stock to be allocated among the various depreciable and non-depreciable assets of Booth distributed to Herald in the liquidation in accordance with the respective fair market values of the assets. Herald allocated $234,063,002 of this amount to various financial assets (cash, securities, including the stock of *Parade*, and accounts and notes receivable); and to tangible assets (land, improvements to land, buildings, production and office equipment, furniture, fixtures, vehicles, computer hardware and software). Herald allocated the remaining $94,110,152 to three intangible assets—$26,337,152 to goodwill and going-concern value combined, and $67,773,000 to a category Herald denominated as "paid subscribers." The amount earmarked as paid subscribers represented Morning Ledger's estimate of the future profits to be derived from the 460,000 at-will subscribers acquired from Booth, all or most of whom were expected to continue to subscribe to the various newspapers after the change in control.

Beginning with its 1977 tax return, Herald claimed depreciation deductions for various assets acquired in the liquidation of Booth. Consistent with applicable regulations, discussed *infra*, Herald did not attempt to claim

Jackson Citizen Patriot; Kalamazoo Gazette; Muskegon Chronicle; and the *Saginaw News*. In addition, Booth owned the stock, valued at roughly $100 million, of the company that published the nationally-distributed Sunday newspaper magazine supplement *Parade*.

depreciation deductions for goodwill or going concern value. On its 1977 through 1980 returns, however, Herald claimed as depreciation deductions a portion of the $67,773,000 amount allocated to paid subscribers. The Service disallowed these deductions on the ground that the amount allocated to paid subscribers should have been included in the amount allocated to non-depreciable goodwill. The Service therefore determined that Herald owed additional taxes and interest for each of the applicable years, which Herald paid in full.

Morning Ledger, as successor to Herald, filed a timely claim for refund with the Service in 1988. After the Service failed to act upon the claim within the six month period prescribed by I.R.C. § 6532(a), Morning Ledger filed the instant action, in the district court for the District of New Jersey, to recover federal income taxes and interest erroneously assessed and collected.

The district court conducted a bench trial at which Morning Ledger argued that, under the relevant regulations and case law, discussed *infra*, in order to depreciate the paid subscribers as an intangible asset, it need only prove that the 460,000 at-will subscriber relationships acquired from Booth: (1) had limited useful lives that could be estimated with reasonable accuracy; and (2) also had ascertainable values separate and distinct from goodwill. Under Morning Ledger's interpretation of these requirements, depreciation deductions were available provided it could satisfy the essentially statistical and factual burden of demonstrating that the subscriber relationships had limited useful lives and that they had ascertainable values.

To this end, Morning Ledger presented the testimony of financial and statistical experts who explained that, based on historical and demographic data, and taking due consideration of actuarial factors such as death, relocation, changing life-styles and tastes, and competition from other media sources, they had arrived at reasonable estimates

of how long the average at-will subscriber existing in 1977 would continue to subscribe to the various newspapers. These estimates ranged from a low of 14.7 years for subscribers to the *Ann Arbor News* to a high of 23.4 years for subscribers to the *Bay City Times*.

These experts further testified that, from among the market, cost, and income approaches to valuing the existing subscriber relationships in 1977, the income approach provided the only appropriate methodology. Employing this approach, the experts testified that they first calculated the present value of the gross revenue stream that would be generated by these subscribers over their estimated useful lives. From this amount, they subtracted the projected costs of collecting that subscription revenue. The experts opined that the resultant net revenue stream, estimated by one expert as $67,773,000 and by another as $60,470,000, represented a reasonable estimate of the value of the intangible asset designated as paid subscribers.

For the most part, the Service did not contest Morning Ledger's expert evidence. Indeed, the Service stipulated to Morning Ledger's estimates of the useful lives of the subscription relationships. It did contest Morning Ledger's reliance on the *income* method of valuation, arguing that, assuming that the asset was depreciable at all, the *cost* method was the only appropriate method, and that the cost of generating 460,000 subscribers through a subscription drive was on the order of only $3 million. The Service refused, however, despite the district court's entreaties, to present expert evidence to refute Morning Ledger's estimates of the value of the subscriber relationships under the income method.[2]

[2] As noted, in valuing the subscriber relationships under the income method, Morning Ledger's experts reduced the present value of the anticipated gross income stream only by the projected costs of collecting subscription fees. The district court was concerned that Morning Ledger had overstated the value of the subscriber relationships by failing to reduce the projected gross income stream from the subscribers by a pro-rata portion of the newspapers' editorial and production costs and overhead. Morning Ledger argued, in justifying its valuations, that the eight newspapers derived upwards of 80 percent of their total revenues from advertising fees. Thus, Morning Ledger argued, all the costs of putting together and printing the newspapers were expended to generate this advertising revenue. The roughly 20 percent of total revenues generated by subscribers was, under Morning Ledger's theory, essentially "gravy" and thus should be viewed as being generated without additional cost other than collection costs. The district court was suspicious, in our view justifiably so, of this reasoning. But the government refused to provide contradictory expert valuation under the income method. Eventually, Morning Ledger's expert who had originally calculated the value of the subscription relationships at $67,773,000 testified that even assuming a pro-rata allocation of costs and overhead, their value would be reduced only to $61,500,000. *See* 734 F. Supp. 176, 182.

The crux of the Service's case, rather, was that Morning Ledger had misinterpreted the applicable law and that all its sophisticated financial and statistical evidence was therefore irrelevant to the fundamental legal hurdle which it could not overcome. That hurdle, in the Service's submission, is that governing law requires a taxpayer to do more than demonstrate a reasonable estimate of useful life and an ascertainable value in order to depreciate a purchased intangible asset; in addition, the taxpayer is required to demonstrate that the asset *is not goodwill*. In the Service's view, the future stream of revenues expected to be generated by the existing 460,000 at-will subscribers is the very essence of the goodwill value of the newspapers and, as such, is not depreciable.

The district court rejected the Service's argument, holding, in effect, that any asset for which a useful life could be demonstrated and a value ascertained was, by definition, not goodwill. Having reached this conclusion, and having no expert evidence before it but that of Morning Ledger, the court held that Morning Ledger was entitled to depreciate the paid subscribers account over its esti-

mated useful lifetime based on a total value of $67,773,000, which amount the court allocated to the various daily and Sunday newspapers. The court ordered the parties to calculate, and the government to repay, all taxes erroneously paid by Morning Ledger and applicable interest thereon.

The Service timely appealed from the final judgment of the district court. We thus have jurisdiction pursuant to 28 U.S.C. § 1291. Determining whether a taxpayer has satisfied the requirements for depreciating an intangible asset is generally a factual question. *See Manhattan Co. of Virginia, Inc. v. Commissioner*, 50 T.C. 78, 92-93 (1968). Hence, we review the district court's factual findings for clear error. Of course, to the extent that the district court misinterpreted or misconstrued the governing law, our review is plenary.

II. DISCUSSION

A. *The Regulations, The Nature of Goodwill, and the Contentions of the Parties*

I.R.C. § 167(a) allows as a depreciation deduction a reasonable allowance for exhaustion, wear and tear, and obsolescence of property, both tangible and *intangible*, used in a trade or business. Treasury Regulation 1.167(a)-3 elaborates on the depreciation of intangibles as follows:

> If an intangible asset is known from experience or other factors to be of use in the business or in the production of income for only a limited period, the length of which can be estimated with reasonable accuracy, such an intangible asset may be the subject of a depreciation allowance. Examples are patents and copyrights. An intangible asset, the useful life of which is not limited, is not subject to the allowance for depreciation. No allowance will be permitted merely because, in the unsupported opinion of the taxpayer, the intangible asset has a limited useful life. *No deduction for depreciation is allowable with respect to goodwill. . . .*

26 C.F.R.§ 1.167(a)-3 (emphasis added).

Case law interpreting this regulation has held consistently that, in order to qualify for depreciation of an intangible asset, a taxpayer must establish that the intangible asset (1) has an ascertainable value *separate and distinct from goodwill*, and (2) has a limited useful life, the duration of which can be ascertained with reasonable accuracy. *See, e.g., Houston Chronicle Publishing Co. v. United States*, 481 F.2d 1240, 1250 (5th Cir. 1973), *cert. denied*, 414 U.S. 1129, 94 S.Ct. 867, 38 L. Ed. 2d 754 (1974).[3]

As we have noted, the Service essentially concedes that Morning Ledger has demonstrated that the paid subscribers have an ascertainable value and limited useful lives, and that it has presented a reasonably accurate estimate of these useful lives. In Morning Ledger's view, detailed *infra*, this concession should end the case. The Service argues, however, that Morning Ledger has ignored, and convinced the district court to ignore, the additional requirement that the value of the paid subscribers be shown to be *"separate and distinct from goodwill,"* consistent with the explicit statement in the regulations that *"[n]o deduction for depreciation is allowable with respect to goodwill."* This prohibition against depreciating goodwill, the Service notes, is nearly as old as the income tax itself, its origin being traceable to a 1927 amendment to the predecessor regulation of § 1.167(a)-3.[4]

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[3] The Service itself adopted the *Houston Chronicle* test shortly after its publication. *See* Rev. Rul. 74-456, 1974-2 C.B. 65.

[4] As amended, the predecessor to § 1.167(a)-3 read:

> Intangibles, the use of which in the trade or business is definitely limited in duration, may be the subject of a depreciation allowance. Examples are patents and copyrights. Intangibles, the use of which in the trade or business is not so limited, will not

The Service further argues that, once we recognize that the district court ignored this requirement, the error of permitting Morning Ledger to depreciate the net income stream to be generated by the 460,000 at-will subscribers becomes evident. Morning Ledger cannot demonstrate that this income stream is separate and distinct from goodwill, the Service contends, because, in fact, it is the essence of goodwill. Although goodwill is not defined in the regulations,[5] it has been repeatedly characterized in the case law

usually be a proper subject of such an allowance. If, however, an intangible asset acquired through a capital outlay is known from experience to be of value in the business for only a limited period, the length of which can be estimated from experience with reasonable certainty, such intangible asset may be the subject of a depreciation allowance, provided the facts are fully shown in the return or prior thereto to the satisfaction of the Commissioner. *No deduction for depreciation, including obsolescence, is allowable in respect of goodwill.*

T.D. 4055, VI-2 CB 63; Regulations 69, Art. 163 (Revenue Act of 1928) (emphasis added). This amendment followed the decision in *Red Wing Malting Co. v. Willcuts*, 15 F.2d 626 (8th Cir. 1926), *cert. denied*, 273 U.S. 763, 47 S. Ct. 476, 71 L. Ed. 879 (1927), which denied a depreciation deduction for lost goodwill to a distillery forced out of business by Prohibition.

[5] As we have noted, the governing regulations have prohibited the depreciation of goodwill for over sixty years. *See supra* note 3. During that time, the meaning of the term "goodwill" has been litigated repeatedly, and often with high stakes, as taxpayers attempt to minimize the tax burden associated with purchased intangible assets by minimizing the amount of the purchase price allocated to nondepreciable goodwill. Despite the recurrence of the issue, neither Congress, the Treasury, nor the Service has seen fit to promulgate a uniform or coherent definition of the term. Rather, the Service apparently has been content to permit the courts to wrestle, case-by-case, with the contours of this elusive concept, with the result that it wins most cases because the taxpayer cannot sustain the onerous burden of establishing value and determinable life.

We note that the absence of a clear definition of this critical term, and the resulting confusion in applying the regulations, have generated much criticism among the commentators. *See* Mundstock, *Taxation of Business Intangible Capital*, 135 U. Pa. L. Rev. 1179, 1206-07 (1987);

as "the expectancy that old customers will resort to the old place," *Commissioner v. Killian*, 314 F.2d 852, 855 (5th Cir. 1963), and as "the expectancy of continued patronage, for whatever reason," *Boe v. Commissioner*, 307 F.2d 339, 343 (9th Cir. 1962). Because the projected stream of income to be generated by the 460,000 at-will subscribers is simply a quantification of Morning Ledger's expectation that these subscribers will continue their patronage, the Service submits that the amount is a portion of the total non-depreciable goodwill purchased from Booth.

We note in this regard, and the Service does not dispute, that the value of the paid subscribers would not constitute goodwill if Morning Ledger's "expectation of continued patronage" were contractually-based. *See Commissioner v. Seaboard Finance Co.*, 367 F.2d 646, 649 (9th Cir. 1966) ("[G]oodwill [is] 'the probability that old customers will resort to the old place' without contractual compulsion.") (citation omitted). Thus, if the subscribers were contractually obligated to continue subscribing for some period of time, Morning Ledger clearly would be permitted to depreciate the value of those contracts over

Dubin, *Allocation of Costs to, and Amortization of, Intangibles in Business Acquisitions*, 57 Taxes 930, 933 (1979); Grigsby & Cotter, *Amortization of Certain Intangibles*, 30 U.S.C. Tax Inst. 543, 545 (1978); Gregorcich, *Amortization of Intangibles: A Reassessment of the Tax Treatment of Purchased Goodwill*, 28 Tax Law. 251, 258-59 (1975); Frank, *Goodwill is Not Immortal: A Proposal to Deduct The Exhaustion of Purchased Goodwill*, 23 J. Taxation 380, 380-81 (1965); Note, *An Inquiry Into the Nature of Goodwill*, 53 Colum. L. Rev. 660, 685-86 (1953). For the views of other commentators who have examined this troublesome corner of the tax law, *see* B. Bittker & L. Lokken, *Federal Taxation of Income, Estates and Gifts* ¶ 23.2.6, at 23-35 (2d ed. 1989); Comment, *Depreciability of Going Concern Value*, 122 U. Pa. L. Rev. 484 (1973); Note, *Amortization of Intangibles: An Examination of the Tax Treatment of Purchased Goodwill*, 81 Harv. L. Rev. 859 (1968); Schenk, *Depreciation of Intangible Assets: The Uncertainty of Death and Taxes*, 13 Wayne L. Rev. 501 (1967).

that time period. In such an event, continued patronage would not be a mere "expectation," but a contractual right, and hence not goodwill. In the case at bar, however, all the subscribers are *terminable-at-will*. At the time of the acquisition of Booth, therefore, Herald merely expected continued patronage; it had no contractual right to demand it. Morning Ledger responds that it has not ignored the requirement that the paid subscribers be shown to have a value "separate and distinct from goodwill." Rather, Morning Ledger contends, the Service has invoked the wrong definition of "goodwill" and thus has misconstrued the requirements of § 1.167(a)-3. Morning Ledger argues that, properly defined, goodwill is no more than the residual value that remains after all assets with determinable useful lives and ascertainable values have been accounted for. Thus, by converse reasoning, anything possessing a determinable useful life and an ascertainable value is not goodwill.[6] Under Morning Ledger's definition of goodwill, in other words, the requirement that an intangible asset be shown to have a value "separate and distinct from goodwill" adds nothing to the undisputedly satisfied requirement that the taxpayer demonstrate that the asset has a limited useful life and provide a reasonably accurate estimate of that life.

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[6] Morning Ledger makes this argument most forcefully in the following passage in its brief:

> The government recognizes that a "basic premise of the Regulation [§ 1.167(a)-3]" is "that goodwill has an indeterminate useful life." Given this basic premise, an asset with a "determinate" useful life cannot be goodwill under the regulation. Nevertheless, the government attempts to define "goodwill" to include any intangible customer base asset acquired as part of a going concern, "even if it could be shown in a given case to have a finite duration." Not surprisingly, the government cites no authority for this "inference." To the contrary, . . . if an asset has a limited useful life, by definition it is no longer goodwill for purposes of depreciation.

Appellee's Brief at 32-33 (citations omitted).

Although the district court apparently sought to reconcile the competing definitions of goodwill, it is clear from the following passage that ultimately the court accepted the definition advanced by Morning Ledger over that pressed by the Service:

> [T]he court recognizes and accepts that goodwill is the expectancy that former customers will be retained—that there will be continued patronage. However, one must distinguish between a galaxy of customers who may or may not return, whose frequency is unknown, and whose quantity and future purchases cannot be predicted, against subscribers who can be predicted to purchase the same item, for the same price on a daily basis. Although newspaper subscribers are under no legal obligation to continue their subscriptions, expert opinion and the evidence presented coupled with common sense and experience leads inescapably to the conclusion that the income derived from such paying subscribers will recur, which, in turn, permits the ascertainment of value separate and apart from goodwill. The income derived from the subscribers permits the calculation of value over the useful lives of the subscriptions or subscribers, and renders the subscribers acquired subject to valuation as an asset separate and apart from goodwill.

Newark Morning Ledger Co. v. United States, 734 F. Supp. 176, 176-77 (D.N.J. 1990).

B. *The Newspaper Subscriber List Cases*

In furtherance of their respective arguments, the parties call our attention principally to two cases that have considered the depreciability of acquired subscriber lists in the context of a newspaper acquisition. Because these two cases present a useful vehicle for framing the instant dispute, we will consider each in some detail.

The Service places substantial emphasis on the Fifth Circuit's decision in *Houston Chronicle Publishing Co. v.*

United States, 481 F.2d 1240 (5th Cir. 1973), *cert. denied*, 414 U.S. 1129, 94 S.Ct. 867, 38 L. Ed. 2d 754 (1974), as an example of the correct application of § 1.167(a)-3 to determine the tax consequences of an acquisition such as the one before us. That case arose from a transaction in which the plaintiff, the publisher of the *Houston Chronicle*, paid $4.5 million for various assets, including a list of 89,000 subscribers, of its former competitor, the *Houston Press*, upon cessation of the latter's activities as a going concern. After the purchase, the *Chronicle* estimated that it would be able to use the list to contact and solicit new subscriptions from 35,600 former *Press* subscribers. Estimating further that previously it had spent roughly $2 to identify and solicit each new subscriber, the *Chronicle* assigned a value to the list of $71,200 and claimed depreciation deductions against this amount under § 167(a).

The Service disallowed the deduction on the ground that the customer list was nondepreciable under the so-called "mass asset rule," a now outdated, but then prevalent, doctrine which requires brief explanation. Until 1973, the Service successfully had persuaded the courts that documentary evidence of customer structure, such as a customer list, was generally sufficiently intertwined with goodwill, if not goodwill itself, so as to render depreciation inappropriate as a rule-of-thumb. There emerged, in support of this result, the mass asset or indivisible asset doctrine, a sort of legal fiction that customer lists, and other documentary evidence of customer structure, are presumed like goodwill to be self-regenerating and *per se* nondepreciable.[7]

[7] Perhaps the most comprehensive statement of the theory behind the mass asset doctrine is found in *Golden State Towel and Linen Service, Ltd. v. United States*, 373 F.2d 938, 179 Ct. Cl. 300 (1967). In that case, the Court of Claims invoked the doctrine in affirming the Service's denial of depreciation deductions claimed by a linen service corporation that had acquired all of the assets of two competitors, and then sought to capitalize the portion of the purchase price attributable to acquired customer lists. The court stated:

> [Plaintiff seeks] an implausible separation of customer lists from goodwill, one a mirror reflection of the other, for goodwill = expectancy of continued patronage = customer lists = goodwill. At least, if goodwill and customer lists are not mutually coextensive, the former includes the latter, and the lesser is inextricable from the greater. In the vernacular, goodwill is a customer list with trimmings. . . .
>
> [A] purchased terminable-at-will type of customer list is an indivisible business property with an indefinite, nondepreciable life, indistinguishable from—and the principal element of—goodwill, whose ultimate value lies in the expectancy of continued patronage through public acceptance. It is subject to temporary attrition as well as expansion through departure of some customers, acquisition of others, and increase or decrease in the requirements of individual customers. A normal turnover of customers represents merely the ebb and flow of a continuing property status in this species, and does not within ordinary limits give rise to the right to deduct for tax purposes the loss of individual customers. The whole is equal to the sum of its fluctuating parts at any given time, but each individual part enjoys no separate capital standing independent of the whole, for its disappearance affects but does not interrupt or destroy the continued existence of the whole.

Id., 373 F.2d at 942-44. For examples of other applications of the mass asset doctrine, *see Thoms v. Commissioner*, 50 T.C. 247 (1968) (denying depreciation of list of insurance expirations purchased in conjunction with sale of insurance agency as going concern on ground that list was "inextricably linked with goodwill" of seller under mass asset doctrine); *Marsh & McLennan, Inc. v. Commissioner*, 420 F.2d 667 (3d Cir. 1969) (affirming Tax Court's denial of depreciation deductions for acquired insurance expirations under mass asset rule); *Skilken v. Commissioner*, 420 F.2d 266 (6th Cir. 1969) (affirming Tax Court's denial of depreciation for 922 acquired oral, terminable at-will location agreements for vending machines on ground that such agreements were comparable to customer lists and thus nondepreciable as inextricably intertwined with goodwill under mass asset doctrine).

The *Houston Chronicle* filed a refund suit, contesting the Service's determination in federal district court. A jury trial was held, the *Chronicle* prevailed, and the Service appealed. The Fifth Circuit affirmed. Specifically, after re-

viewing many of the prior cases and reaffirming the definition of goodwill as "the expectancy that the old customers will resort to the old place," and "the expectancy of continued patronage, for whatever reason," *see supra* at [11a], the court concluded, essentially rejecting the mass asset rule, that the government was incorrect in asserting that the "subscription lists [were] non-amortizable as a matter of law." *Id.* at 1248. In the passage that has become the standard for all subsequent related cases, the court went on to state:

> Without compiling the myriad cases that discuss the "mass asset" rule, we are satisfied that the rule does not establish a *per se* rule of non-amortizability in every case involving both goodwill and other intangible assets. In the light of § 167(a) of the Code and Regulation § 1.167(a)-3, we are convinced that the "mass asset" rule does not prevent taking an amortization deduction if the taxpayer properly carries his dual burden of proving that the intangible asset involved (1) has an ascertainable value separate and distinct from goodwill, and (2) has a limited useful life, the duration of which can be ascertained with reasonable accuracy.

Id. at 1249-50.

It is clear from this passage, the Service contends, that the two-pronged test articulated by *Houston Chronicle* was intended to inter the notion that some intangible assets, although not necessarily goodwill, were nonetheless so intertwined with goodwill as to be nondepreciable as a matter of law in all cases—i.e., the mass asset rule. The Service adds, however, that there is no indication in *Houston Chronicle* that the court intended to hold that goodwill itself was depreciable or to replace what it had confirmed to be the traditional definition of goodwill with the residual definition such as is urged by Morning Ledger in the instant dispute. Rather, the Service contends, the court

merely held that in those cases where a taxpayer could demonstrate, as a factual matter, that an intangible asset such as a subscriber list was "separate and distinct" from the legal concept of goodwill—i.e., the "expectancy that old customers will resort to the old place," it ought to be permitted to do so.

As a factual matter, the Service adds, the circumstances supporting the finding that the taxpayer in *Houston Chronicle* had demonstrated that the subscriber list was "separate and distinct" from goodwill are clearly distinguishable from the instant dispute. The *Houston Chronicle* did not purchase an ongoing business or even a tradename as did Morning Ledger, but rather the idle assets of the defunct *Houston Press*. Hence, there was no "expectancy that old customers would resort to the old place" because "the old place" no longer existed. The value of the customer list to the *Houston Chronicle* therefore lay solely in its potential use as a marketing tool to solicit *new* customers to a *new* business. As such, the asset was appropriately valued at the *cost* of generating a comparable list of potential subscribers, not, as Morning Ledger has attempted, as the entire net stream of *income* such subscribers would generate if obtained. In short, the Service argues that, unlike the present dispute, there was no goodwill transferred in the acquisition of the assets of the *Houston Press* and thus no risk that goodwill would be bound up and depreciated along with the subscriber list.

In sum, contends the Service, *Houston Chronicle* presented the paradigmatic circumstances under which a taxpayer could demonstrate that a subscriber list is "separate and distinct from goodwill." The Service argues that the instant dispute, by contrast, presents a clear case wherein it is virtually impossible for the taxpayer to disentangle the potentially depreciable value of the list from the value of the nondepreciable goodwill transferred. In any event, on the record as it stands, and particularly in light of Morning Ledger's insistence on employing the income

method of valuation, the Service argues that Morning Ledger clearly has not demonstrated that the $67,773,000 value it assigned to the list is "separate and distinct from goodwill."

Morning Ledger advances as its strongest authority the Eighth Circuit's decision in *Donrey, Inc. v. United States*, 809 F.2d 534 (8th Cir. 1987). Although a much smaller transaction in absolute dollar terms than the acquisition of Booth by Morning Ledger, the case is undeniably similar to the instant dispute in terms of the material aspects of the transaction. Specifically, in *Donrey* the taxpayer purchased a small Indiana newspaper with roughly 11,000 at-will subscribers for $1,335,804 and as a going concern. The taxpayer assigned $559,406 to the newspaper's customer list/customer structure and attempted to depreciate that amount over 23 years. Although the case is not explicit on this point, it is reasonable to assume, given the amount allocated to the customer list relative to the total purchase price, that this amount was calculated under the income, rather than cost method, of valuation.

When the Service denied the depreciation deductions on the theory that the taxpayer was seeking to depreciate goodwill, the taxpayer sued for a refund in district court and demanded a jury trial. The case was submitted to the jury on special interrogatories tracking the standards of *Houston Chronicle*, and the taxpayer prevailed. A divided Eighth Circuit panel rejected the government's appeal.

The Eighth Circuit majority's reasoning is somewhat cursory, and is largely premised on the substantial deference due the jury's determination that the taxpayer had proved a value separate and distinct from goodwill. *Donrey*, 809 F.2d at 536-37. Morning Ledger argues convincingly, however, that the majority's reasoning implicitly adopted the residual definition of goodwill urged by Morning Ledger here. Indeed, this reading of the case is confirmed by Judge Bright's eloquent dissent, which takes the

majority to task for ignoring the traditional definition of goodwill, and in so doing, for concluding wrongly that the taxpayer had demonstrated that the value of the customer structure was "separate and distinct from goodwill." *Id.* at 537-39 (Bright, J., dissenting).

C. *The Case Law in Overview*

It would appear that *Houston Chronicle* and *Donrey* are directly in conflict. Before charting our own course, it therefore behooves us to look beyond the cases involving newspaper subscriber lists to the plethora of other cases that have considered the depreciability of customer or subscriber lists in other industries. This exercise, we believe, clearly indicates that the case law division is greatly overstated by Morning Ledger. Viewed in the context of the case law as a whole, there is undeniably some authority consistent with *Donrey* and supportive of the argument advanced by Morning Ledger. The overwhelming weight of the authority, however, lines up squarely behind the Service's reading of *Houston Chronicle*. Given the amount of ink that has been spilled over this subject already both in the literature, *see supra* [13a-15a], and in the case law, we will not survey the case law in detail. The following review of some of the better authorities should suffice.

Several cases support, to some degree or another, Morning Ledger's argument that any intangible asset which possesses a determinable useful life and which is capable of valuation is not goodwill. For example, a line of cases from the Court of Claims comes very close to adopting Morning Ledger's definition of goodwill. *See Meredith Broadcasting Co. v. United States*, 405 F.2d 1214, 1224-25, 186 Ct. Cl. 1 (1968); *KFOX, Inc. v. United States*, 510 F.2d 1365, 1376-77, 206 Ct. Cl. 143 (1975); *Richard S. Miller & Sons, Inc., v. United States*, 537 F.2d 446, 450-54, 210 Ct. Cl. 431 (1976). Perhaps the clearest statement of the Court of Claims' view is found in the following passage from *Richard S. Miller*:

The term "goodwill" has a varying content, depending on its usage. Goodwill sometimes is used to describe the aggregate of all of the intangibles of a business, including such items as patents, trademarks, leases, contracts, and franchises. Since a normal rate of return usually is calculated on tangible assets only, goodwill has been used as a synonym for the return on all the intangibles of a business. In a more restricted sense, goodwill is the expectancy that the old customers will resort to the old place. It is the sum total of all the imponderable qualities that attract customers and bring patronage to the business without contractual compulsion. Another definition equates goodwill with a rate of return on investment which is above normal returns in the industry and limits it to the residual intangible asset that generates earnings in excess of a normal return on all other tangible and intangible assets. *In this court for tax purposes, the intangible value of a business is divisible into its identifiable constituent elements. . . . The most significant indication that an intangible asset is separate and distinct from goodwill is whether its useful life can be shown with reasonable accuracy to be of limited duration. The most important criterion is whether in fact it is a wasting asset.*

Richard S. Miller, 537 F.2d at 450-52 (citations omitted) (emphasis added).

There are also a few cases that, like *Donrey*, provide implicit, and consequently somewhat less persuasive, authority for Morning Ledger's asserted definition of goodwill. In *Super Food Services, Inc. v. United States*, 416 F.2d 1236 (7th Cir. 1969), for example, the taxpayer, who had purchased a supermarket chain as ongoing business, was permitted to depreciate, as an intangible asset, 184 terminable-at-will retail franchise contracts acquired as part of the deal. The implicit reasoning of the court was that,

having demonstrated that the contracts had limited useful lives, and having provided a reasonable estimate of those lives, the taxpayer was not obligated further to prove that the contracts were distinct from the goodwill value of the acquiree. *See also Business Service Industries, Inc. v. Commissioner*, 51 T.C.M. (CCH) 539, 543 (1986) (upholding taxpayer's claimed depreciation deductions for acquired terminable-at-will MUZAK customer contracts on implicit ground that it was sufficient that taxpayer had demonstrated that contracts had ascertainable value and useful life).

Still other cases appear confused in their analyses, ultimately providing support for both conflicting definitions advanced in the case at bar. In *Los Angeles Central Animal Hospital, Inc. v. Commissioner*, 68 T.C. 269, 273-74 (1977), for example, the Tax Court noted, consistent with the Service's position here, that goodwill is typically defined as the expectancy that "old customers will resort to the old place of business." *Id.* at 273 (citations omitted). Seemingly switching definitions of goodwill in midstream, the court then held that the taxpayer could depreciate the cost of 12,000 medical record cards purchased as part of the sale of a veterinary practice.

> From those [medical] records, the operator of the business is able to generate business by contacting the pet owners whose animals require periodic immunization and innoculation. The "repeat business" which was obtained through the use of these records was not dependent solely on the normal elements of "goodwill." These specific records do not retain their value indefinitely as part of the continuing operation of the practice.

Id. at 274.

The strongest authority mustered by Morning Ledger in support of its argument is the recent memorandum decision of the Tax Court in *Colorado National Bank-*

shares, Inc. v. Commissioner, 60 T.C.M. (CCH) 771 (1990).[7a] The case involved the depreciability of so-called "core deposits" (i.e., checking account and saving account deposits) following the acquisition of the assets and accounts of one bank by another. On the theory that such deposits represent a valuable source of prospective income to a bank—inasmuch as the deposits are obtained at no or relatively low cost but can be continuously reinvested by the bank at higher rates of return—the acquiror bank sought to depreciate the portion of the purchase price attributable to the core deposits as an intangible asset. In an attempt to satisfy the requirements of § 1.167(a)-3, the acquiror bank employed sophisticated financial and statistical methods to estimate the average length of time that depositors would maintain their deposits and, based on these estimates, to calculate the total net value of the core deposits.

The Service responded that, in effect, the acquiror bank was attempting to depreciate the value of its expectation that the depositors would continue to patronize the bank—i.e., the value of the goodwill of the acquired bank. The Tax Court rejected the Service's position, clearly adopting the view that any intangible asset possessing a determinable life and an ascertainable value is, by definition, not goodwill.

> Goodwill, by definition, has an indefinite life and is valued using the residual method. By contrast, the deposit accounts of the acquired banks could be, and were, identified; had limited lives that could be estimated with reasonable accuracy; and could be, and have been, valued directly with a fair degree of accuracy. Moreover, petitioner's deposit accounts were not self-regenerating. Therefore, the deposit accounts were assets with values separate and apart from goodwill. It is these characteristics which separate them from general goodwill and permits separate valuation. We conclude that petitioner has proven that the core deposits intangible at issue here has an ascertainable cost basis separate and distinct from the goodwill and going-concern value of the acquired banks.

[7a] The parties called to our attention in the Petition for Rehearing that the Eleventh Circuit has, in a published opinion, summarily affirmed the reasoning of a published Tax Court Opinion, *Citizens & Southern Corp. v. Commissioner*, 91 T.C. 463 (1988), *aff'd*, 919 F.2d 1492 (11th Cir. 1990) (per curiam), which essentially tracks the reasoning of *Colorado National*. Although there now appears to be a Circuit split on this issue, for the reasons set forth in the text, we respectfully disagree with the Eleventh Circuit's position.

Colorado National, 60 T.C.M. (CCH) at 789 (citations omitted).

We could attempt to distinguish *Colorado National* and *Citizens & Southern* from the instant dispute. We believe, however, that such an exercise ultimately would prove pointless and would be somewhat disingenuous. The unavoidable fact is that there does exist authority bolstering Morning Ledger's position.

It is equally clear, however, that *Colorado National* and the other cases referenced by Morning Ledger represent no more than a minority strand amid the phalanx of cases that have considered the definition and application of the term "goodwill" in the context of § 1.167(a)-3, and which support the Service's position. *See, e.g., Brooks v. Commissioner*, 36 T.C. 1128, 1133 (1961) (defining goodwill as " 'the probability that old customers will resort to the old place' " (quoting *Horton v. Commissioner*, 13 T.C. 143, 148 (1949), *acq. and petition dismissed*, 180 F.2d 354 (10th Cir. 1950))); *Boe v. Commissioner*, 307 F.2d 339, 343 (9th Cir. 1962) ("essence of good will is the expectancy of continued patronage, for whatever reason"); *Nelson Weaver Realty Co. v. Commissioner*, 307 F.2d 897, 901 (5th Cir. 1962) ("good will [is] the probability that the old customers will resort to the old place"); *Commissioner v. Killian*, 314

F.2d 852, 855 (5th Cir. 1963) (quoting *Nelson Weaver*); *Commissioner v. Seaboard Finance Co.*, 367 F.2d 646, 649 (9th Cir. 1966) (quoting *Boe* and *Brooks*); *Golden State Towel and Linen Service, Ltd. v. United States*, 373 F.2d 938, 941, 179 Ct. Cl. 300 (1967) (quoting *Boe*); *Skilken v. Commissioner*, 420 F.2d 266, 270 (6th Cir. 1969) (" '[Goodwill] . . . is constituted in the tendency of customers to return for trade to those with whom they are accustomed to deal.' " (quoting *Burke v. Canfield*, 121 F.2d 877, 880 (D.C. Cir. 1941)); *Winn-Dixie Montgomery, Inc. v. United States*, 444 F.2d 677, 681 (5th Cir. 1971) ("[G]oodwill is acquired by the purchaser of a going concern where the 'transfer enables the purchaser to step into the shoes of the seller,' " (quoting *Balthrope v. Commissioner*, 356 F.2d 28, 32 n.1 (5th Cir. 1966)); *Houston Chronicle Publishing Co. v. United States*, 481 F.2d 1240, 1247 (5th Cir. 1973), *cert. denied*, 414 U.S. 1129, 94 S. Ct. 867, 38 L. Ed. 2d 754 (1974) (quoting *Nelson Weaver, Boe,* and *Balthrope*); *Robins & Weill, Inc. v. United States*, 382 F. Supp. 1207, 1214 (M.D.N.C. 1974) (quoting *Killian*); *Computing & Software, Inc. v. Commissioner*, 64 T.C. 223, 233 (1975), *acq.*, 65 T.C. 1153 (1976) (essence of goodwill is a preexisting business relationship, based on a continuous course of dealing, which may be expected to continue indefinitely); *Los Angeles Central Animal Hospital, Inc. v. Commissioner*, 68 T.C. 269, 273 (1977) (citing *Houston Chronicle, Killian, Boe,* and *Computing & Software, Inc.*); *General Television, Inc. v. United States*, 449 F. Supp. 609, 612 (D. Minn. 1977) *aff'd*, 598 F.2d 1148 (8th Cir. 1979) ("the expectancy of continued patronage is the essence of goodwill"); *Illinois Cereal Mills, Inc. v. Commissioner*, 46 T.C.M. (CCH) 1001, 1023 (1983), *aff'd*, 789 F.2d 1234 (7th Cir. 1986), *cert. denied*, 479 U.S. 995, 107 S. Ct. 600, 93 L. Ed. 2d 600 (1986) (citing *Seaboard Finance Co.* and *Computing & Software, Inc.*); *Banc One Corp. v. Commissioner*, 84 T.C. 476, 508 (1985), *aff'd without opinion*, 815 F.2d 75 (6th Cir. 1987) (quoting *Boe*); *Decker v. Commissioner*, 864 F.2d 51, 54 (7th Cir. 1988) (quoting *Winn-Dixie*); *AmSouth Bancorporation and Subsidiaries v. United States*, 681 F. Supp. 698, 712 (N.D. Ala. 1988) (quoting *Houston Chronicle*).

A brief review of the application of this definition to the facts of a few of these cases demonstrates convincingly that the Service has more accurately characterized the prevailing case law in relation to the facts of the current dispute. In *General Television, Inc. v. United States*, 449 F. Supp. 609 (D. Minn. 1977), *aff'd*, 598 F.2d 1148 (8th Cir. 1979), for example, the taxpayer purchased two community antenna television (CATV) stations. Among the assets of the two stations were over 7,000 at-will subscriber contracts, which the taxpayer sought to depreciate as intangible assets. When the Service disallowed the depreciation deductions, the taxpayer paid the tax and filed a refund suit. The district court, viewing the totality of the subscriber contracts as essentially a customer or subscriber list, denied the taxpayer's request stating:

> It is true that certain types of customer or subscriber lists have an ascertainable value separate and apart from goodwill. However, in the instances in which customer or subscriber lists have been determined to have an ascertainable value separate and apart from goodwill, the lists alone carried with them no expectancy of continued patronage. In the present case, what the plaintiff purchased was more than mere subscriber lists which could be used to identify potential customers; what it purchased was customer structures which included the expectancy of continued patronage. Therefore, because the purchases of the subscriber lists were actually purchases of customer structures with the expectancy of continued patronage and because the expectancy of continued patronage is the essence of goodwill, the subscriber lists constitute non-depreciable goodwill.

Id. at 611-12 (citations omitted).

Similarly, in *Panichi v. United States*, 834 F.2d 300 (2d Cir. 1987), the Second Circuit upheld a district court ruling that a taxpayer who purchased a list of customers from a trash collection business was entitled to depreciate the value of the list. The court was careful to note that the list was depreciable because the taxpayer had not acquired it as part of a going concern. Thus, there was no possibility that the value of the list reflected the value of the seller's goodwill. *Id.* at 301-02.[8]

Finally, it is worth noting the decision in *AmSouth Bancorporation and Subsidiaries v. United States*, 681 F. Supp. 698 (N.D. Ala. 1988), a case which, like *Colorado National* and *Citizens & Southern*, considered the depreciability of core deposits, or customer deposit base, in the context of a bank acquisition. By opting for the traditional definition of goodwill in the tax context, *AmSouth* arrives at a hold-

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[8] Additionally, in *Robins & Weill, Inc. v. United States*, 382 F. Supp. 1207 (M.D.N.C. 1974), one of the first cases to apply *Houston Chronicle's* two-pronged standard, the court considered the depreciability of acquired insurance "expirations," which are essentially records of when existing policyholders' coverage will expire and thus of when an opportunity to write new policies will arise. After invoking the oft-repeated definition of goodwill as "the expectancy that old customers will resort to the old place" and "the expectancy of continued patronage, for whatever reason," *Id.* at 1214, the court noted that the taxpayer had purchased expirations from two different agencies. In one of these purchases, the court reasoned, the taxpayer sought the expirations solely for their informational value, and had not purchased the rights to the prior agency's personnel, trade name, business location, or other components of goodwill. The court therefore concluded that these expirations were *not*, in fact, goodwill and thus were depreciable. The purchase of the other agency's expirations, however, was made in conjunction with the complete transfer of the employees, trade name, office location, reputation, and customer structure of the acquired agency. The court therefore was of the view that goodwill of far greater value than the $10 amount claimed by the parties had been transferred in the sale. Consequently, the court held that the taxpayer had failed to satisfy its burden of demonstrating a value for the expirations that was "separate and distinct from goodwill." *Id.* at 1215.

ing directly at odds with the Tax Court's holdings in *Colorado National* at [21a-22a] and *Citizens & Southern*, *see supra* n.8. While we recognize that the validity of *AmSouth* is questionable after the Eleventh Circuit's decision in *Citizens & Southern*, we find the reasoning of *AmSouth* sufficiently persuasive and well-articulated to merit quoting from the case at length.

> When deposits are made, two accounting entries result. First, there is a debit (asset) entry for cash or its equivalent. Second, there is an equal and offsetting credit (liability) entry for the liability to the depositor. Any additional asset must be different from the cash thereby acquired. Its creation must, somehow, result from the expectation that the depositor will allow the cash, or its equivalent, to *remain* as an asset and that earnings will result therefrom. This expectation is akin to, if not tantamount, to the expectancy that "old customers will resort to the old place" of business or continued "customer patronage." The "additional" asset does not just materialize out of nowhere. It is geared to the expectancy of the *continued* deposit relationship (patronage). . . .
>
> For accounting purposes, a bank may be able to "identify" a customer deposit base even though it may not be separate and distinct from goodwill. To the extent that deposits remain after some contractually stipulated period, they result from, "continued patronage." The mere fact that the deposits themselves are identifiable, does not make their *"value"* separate and distinct from goodwill. Other facets of bank activities such as safe deposit "expectations," loan "expectations," etc. could perhaps be similarly "identified" so as to phase out the concept of goodwill. There is no indication that tax law permits or contemplates this result.

Id. at 720 (citations omitted) (emphasis in original).

D. *Conclusion*

We do not deny the analytic force of *Colorado National's* residual approach to defining and calculating goodwill. And there is no doubt that many of the commentators would prefer to see the Service and the case law move in this direction, in contrast to the "expectation of continued patronage" standard to which the Service clings.[9] We would be hard pressed, however, after at least thirty years during which: (1) the Service consistently has advanced its definition; (2) courts have overwhelmingly acquiesced to it; and (3) the Congress, the Treasury and the Service, wherein reside the authority and expertise to undertake such a change, have stood mute, to take it upon ourselves to announce a sudden redefinition of a concept so fundamental to tax accounting. In any case, consistent with the prevailing case law, we believe that the Service is

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[9] The following passage is representative of the position taken by many of the commentators:

> In a sense, "goodwill" may be defined as all intangible commercial advantages which have not been specifically identified, valued and analyzed as to their useful lives. The sphere of acquired competitive advantages began its existence in the tax law as being composed entirely of the element labeled "goodwill." Taxpayers, lured by the prospects of cost recovery through amortization, have been able to peel away at the sphere by utilizing sophisticated and objective methods for determining the purchase price before the acquisition or for allocating the price after the fact. In this way, the taxpayer has been able to identify more and more of the intangible advantages for which he has paid money in excess of the value of tangible assets. If the trend continues, theoretically taxpayers should be able to whittle down the sphere so that the core of goodwill becomes non-existent by identifying and allocating the entire excess price to specific competitive advantages. The [only] obstacle to be hurdled for each newly-identified element will be the burden of proof regarding allocation of value and determinable life.

Gregorcich, *Amortization of Intangibles: A Reassessment of the Tax Treatment of Purchased Goodwill*, 28 Tax Law. 251, 270-71 (1975) (citation omitted).

correct in asserting that, for tax purposes, there are some intangible assets which, notwithstanding that they have wasting lives that can be estimated with reasonable accuracy and ascertainable values, are nonetheless goodwill and nondepreciable. We conclude, in short, that the district court applied the wrong definition of "goodwill."

We conclude additionally that, applying the correct definition of goodwill, it is clear that Morning Ledger has not satisfied its burden of demonstrating that the paid subscribers are "separate and distinct from goodwill." As the cases discussed *supra* demonstrate, the depreciability of customer lists, while no longer *per se* forbidden under the mass asset rule, still is limited to a narrow set of circumstances. Customer lists are generally not depreciable when acquired in conjunction with the sale of the underlying business as a going concern. In the context of the sale of a going concern, it is simply often too difficult for the taxpayer and the court to separate the value of the list *qua* list from the goodwill value of the customer relationships/structure.

Even in those cases where customer lists have been deemed depreciable, the value assigned to the lists has been limited to the *cost* of generating a like list of potential subscribers or customers. As a general matter, the courts have not permitted customer lists to be valued as the stream of *income* to be generated by the listed customers over their remaining years of patronage. We agree. We note, moreover, that this preference for the cost approach over the income approach is not premised merely on some obscure aspect of financial theory. The difference in valuations between the cost and income approach, of course, can be substantial. In this case, the Service offered expert testimony that the 460,000 subscribers to the Booth newspapers could be valued on a cost basis at roughly $3 million, whereas Morning Ledger's experts valued the same subscribers on an income basis at over $67 million! More importantly, this difference in the two valuation ap-

proaches implicates the central legal dilemma at issue. The fact is that, when employed in the context of the sale of an ongoing concern, the income approach to valuing a list of customers inherently includes much or all of the value of the expectancy that those customers will continue their patronage—i.e., the goodwill of the acquired concern.

We do not decide whether Morning Ledger could have argued successfully that it was entitled to assign a reasonable cost basis to the list (e.g., the government's $3 million estimate of what it would cost to generate a similar list as a marketing tool) and to depreciate it as an intangible asset, notwithstanding that the list was acquired as part of a going concern. This argument has never been before the court in this case, even as an alternative claim. Morning Ledger apparently never has been satisfied to seek cost recovery on such a small portion of the premium it paid over the value of Booth's tangible assets. Instead, it gambled on persuading the court of the merits of its view of the definition of goodwill and the related case law in the hopes of securing the right to recover through depreciation some $67 million. In our view, however, under the proper definition of goodwill, the $67 million amount established by Morning Ledger is quite clearly comprised largely, if not exclusively, of amounts properly attributable to goodwill. As such, Morning Ledger has not satisfied its burden of proving a value for its so-called paid subscribers that is separate and distinct from goodwill, and the district court's finding to the contrary is clearly erroneous.

The judgment of the district court will be reversed, and the case remanded with instructions to enter judgment in favor of the United States.

A True Copy:
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Clerk of the United States Court of Appeals
for the Third Circuit

APPENDIX B

Civ. A. No. 88-4846.

United States District Court

D. New Jersey

NEWARK MORNING LEDGER CO., as Successor to the Herald Company, Star Ledger Plaza, Newark, New Jersey 07101,

Plaintiff,

v.

THE UNITED STATES OF AMERICA,

Defendant.

April 3, 1990.

In action contesting disallowance of depreciation deductions, the District Court, Sarokin, J., held that acquisition of existing paying subscribers as part of ongoing group of newspapers warranted tax deduction for depreciation and amortization of value of those subscribers as assets separate and apart from goodwill.

Order accordingly.

* * * * * *

Donald A. Robinson, Albert H. Turkus, Robinson, Wayne & LaSala, Newark, N.J., for plaintiff.

Gregory S. Hrebiniak, Dept. of Justice, Tax Div., Washington, D.C., for Defendant.

OPINION

SAROKIN, District Judge.

Introduction

This action involves the issue of whether the acquisition of existing paying subscribers as part of an ongoing group

of newspapers warrants a tax deduction for the depreciation and amortization of the value of those subscribers as an asset separate and apart from goodwill.

The parties concede that the issue is a factual one, and that in order to prevail plaintiff has the burden of proving that as of May 31, 1977, said subscribers had limited useful lives, the duration of which can be estimated with reasonable accuracy, and ascertainable values separate and apart from goodwill.

The court finds, as more specifically hereinafter set forth, that plaintiff has met its burden. In summary, it is self-evident that the subscribers themselves as of a certain date have limited useful lives, because the subscriptions by necessity will terminate upon the death of their respective subscribers. Secondly, plaintiff has presented competent evidence that the subscriptions also have limited useful lives and will terminate for a variety of other reasons prior to the death of their respective subscribers. Either based upon the inevitable death of the *subscribers* or the statistical evidence submitted by plaintiff and the uncontroverted expert opinions that the *subscriptions* have limited useful lives which can be estimated with reasonable accuracy, plaintiff has clearly established that the paying subscribers (or subscriptions) of the acquired newspapers had limited useful lives, the duration of which can be and has been estimated with reasonable accuracy. Indeed, the parties have entered into a stipulation establishing the useful lives of the subscribers for each of the newspapers involved, in the event that this court finds for the plaintiff.

As to the second prong, the court recognizes and accepts that goodwill is the expectancy that former customers will be retained—that there will be continued patronage. However, one must distinguish between a galaxy of customers who may or may not return, whose frequency is unknown, and whose quantity and future purchases cannot be predicted, against subscribers who can be predicted to purchase the same item, for the same price on a daily basis. Although newspaper subscribers are under no legal obligation to continue their subscriptions, expert opinion and the evidence presented coupled with common sense and experience leads inescapably to the conclusion that the income derived from such paying subscribers will recur, which, in turn, permits the ascertainment of value separate and apart from goodwill. The income derived from the subscribers permits the calculation of value over the useful lives of the subscriptions or subscribers, and renders the subscribers acquired subject to valuation as an asset separate and apart from goodwill.

Discussion

The following shall constitute the court's findings of facts and conclusions of law:

Findings of Fact

Plaintiff, Newark Morning Ledger Co. ("Morning Ledger"), is a corporation organized and existing under the laws of the State of New Jersey with its principal place of business in Newark, New Jersey. Stip. para. a. Morning Ledger is a successor by merger to The Herald Company ("Herald") which, prior to its merger into Morning Ledger, published daily newspapers in eight Michigan communities, *inter alia* (the "Booth newspapers"). Stip. para. b,c.

This income tax case involves Herald's claim to depreciation deductions with respect to assets useful in its business, i.e., the existing relationships with the subscribers of the Booth newspapers acquired on May 31, 1977 (sometimes referred to as the "paid subscribers"). Herald claimed deductions for depreciation with respect to those subscriber relationships when it filed its tax returns for the taxable years 1977 through 1980. The Internal Revenue Service (the "Service") disallowed those deductions,

thereby determining an increased tax liability for Herald for each of those years. The correctness of those depreciation deductions is the subject of this action.

During the period beginning February 12, 1976 and ending November 5, 1976, Herald purchased all the outstanding stock of Booth Newspapers, Inc. ("Booth"). Stip. para. e. Booth was a Michigan corporation with its principal place of business in Ann Arbor, Michigan. Booth published the following daily and Sunday paid-circulation newspapers in eight Michigan communities: Ann Arbor News, Bay City Times, Flint Journal, Grand Rapids Press, Jackson Citizen Patriot, Kalamazoo Gazette, Muskegon Chronicle, and Saginaw News. Stip. para. c. On the May 31, 1977 acquisition date, these newspapers had a total of approximately 460,000 subscribers. Stip. para. j. In addition to publishing the Booth newspapers, Booth owned all the stock of the Parade Publications, Inc. ("Parade"), which published a nationally-distributed Sunday newspaper supplement called *Parade*. Stip. para. c.

Prior to Herald's purchase of Booth, Booth's stock was publicly traded. Herald purchased two blocks of Booth stock through private sales, and later made a tender offer for all of the outstanding stock.

Herald did not obtain an appraisal of any of the Booth assets prior to purchasing the Booth stock. Generally, such appraisals are made subsequent to such a purchase according to Roger J. Grabowski.[1] Before purchasing Booth, however, Herald's officers inquired into the financial and other relevant aspects of Booth's operations and met with Booth's Chief Executive Officer. The decision to purchase the Booth stock and the determination of the price to be paid for that stock were influenced by the fact that the

[1] Mr. Grabowski is an expert in valuation theory and methodology, in particular in the valuation of intangible assets in ongoing businesses, in the media industry among others, and in the valuation of customer base assets.

Booth newspapers were paid-circulation newspapers and by the number of subscribers to those newspapers.

On May 31, 1977, Booth was liquidated into Herald by merger in a transaction governed by sections 332 and 334(b)(2) of the Internal Revenue Code of 1954, as amended (the "Code"). Stip. para. c. Subsequently, on June 30, 1987, Herald was merged into Morning Ledger, making the operations of Herald and Booth unincorporated divisions of Morning Ledger. Stip. para. b.

As a consequence of the liquidation of Booth into Herald, pursuant to the rules set forth at section 1.334-1(c)(4)(vi)(b) of the Treasury regulations, Herald's adjusted tax basis in the Booth stock had to be allocated among the assets of Booth in proportion to their respective fair market values as of May 31, 1977. In filing its tax returns for calendar and taxable years 1977 through 1980, Herald claimed depreciation deductions with respect to the paid subscribers of the Booth newspapers. These deductions were calculated by reference to Herald's adjusted basis in the paid subscribers derived from the application of the foregoing rules. The Service disallowed those deductions. Herald paid the additional taxes and interest determined by the Service to be due. Stip. para. d.

Morning Ledger, as successor to Herald, filed a timely claim for refund of taxes and interest previously paid for taxable years 1977 through 1980. Stip. para. m. Pursuant to section 6532(a) of the Code, the Service had six months in which to act upon the claim before suit could be brought. The six-month period expired without action by the Service. Stip. para. n. Morning Ledger timely filed this action to recover federal income taxes and interest which it alleged were erroneously assessed and collected by the Service for those taxable years. Stip. para. o.

The total fair market value of the assets acquired by Herald in the liquidation of Booth was $313,997,154. Herald's total adjusted tax basis in these assets was

$328,173,154. Stip. para. f. The assets were of three types: (1) cash, cash equivalents, and other financial assets including securities, accounts and notes receivable, and deferred charges and deposits; (2) tangible and intangible assets of the Booth newspapers publishing operations including land, land improvements, buildings, equipment, furniture, fixtures, vehicles, paid subscribers, computer software, going concern value, and goodwill; and (3) the stock of Parade. Stip. para. g.

On May 31, 1977, the fair market values and adjusted tax bases of certain of the assets acquired by Herald in the liquidation of Booth were as follows:

Assets	Fair Market Value	Adjusted Tax Basis
Cash and Equivalents	$ 15,617,042	$ 15,617,042
Securities	37,249,852	39,134,189
Accounts and Notes Receivable	15,046,899	15,046,899
Master Repurchase Agreements	3,100,000	3,100,000
Deferred Charges and Deposits	323,944	340,331
Inventories	3,435,627	3,609,423
Land	4,658,885	4,894,561
Land Improvements	1,721,959	1,809,067
Buildings and Improvements	21,350,237	22,430,269
Production Equipment	17,109,130	17,974,620
Computer Hardware	1,300,435	1,366,219
Furniture and Fixtures	880,775	925,330
Office Equipment	731,195	768,184
Autos and Trucks	234,489	246,351
Computer Software	1,658,000	1,741,872
Stock of Parade	100,000,000	105,058,644

Stip. para. h.

The parties have agreed that on May 31, 1977, the total fair market value of the remaining three intangible assets, i.e., the paid subscribers, the going concern value and goodwill of the papers, was $89,578,685 and the total adjusted tax basis to be allocated pro rata to those assets,

pursuant to section 1.334-1(c)(4)(vi)(b) of the Treasury regulations, was $94,110,152, although the government contests that the paid subscribers were assets separate and apart from goodwill. Stip. para. i.

The parties have stipulated that the value of the going concern and goodwill of Booth newspapers will be determined using the residual method, Stip. para. i., the method of valuation generally utilized by the Service and valuation experts to value such assets, according to Larry D. Berkey.[2] Consequently, this court need not determine, based upon direct evidence, the value of goodwill and going concern. The aggregate fair market value of the going concern and goodwill of the Booth newspapers is the difference between $89,578,685 and the fair market value of the paid subscribers of the Booth newspapers, as determined by this Court, assuming that this Court finds that the paid subscribers are assets separate and apart from goodwill. The adjusted tax basis of the paid subscribers of the Booth newspapers is the same proportion of $94,110,152 as the fair market value of the paid subscribers is of $89,578,685. Stip. para. i. The aggregate adjusted tax basis of the going concern and goodwill of the Booth newspapers is the difference between $94,110,152 and the adjusted tax basis of the paid subscribers of the Booth newspapers. Stip. para. i.

All of the foregoing facts are admitted and undisputed. As to the remaining facts in dispute, the court makes the following specific findings:

Advertising provides approximately eighty percent of most newspapers' revenues, including the Booth newspapers. In order to earn advertising revenue, newspapers

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[2] Mr. Berkey also is an expert in valuation theory and methodology, in particular in the areas of the valuation of intangible assets in ongoing businesses, in the media industry among others, and in the valuation of customer base assets.

are required to produce a newspaper that contains news, entertainment and advertising that is interesting to the readers, according to Dr. Christine D. Urban.[3] Some newspapers generate subscription revenue; others do not.

There are basically two types of newspapers, those with a paid circulation, where the newspapers are sold to the readers, and those which are known as free-distribution newspapers, which are provided to the readers without any charge. Within both categories, there are daily newspapers and newspapers published on a less frequent basis, such as weekly, although free daily newspapers are very rare. Included in the two types of newspapers are shoppers, mailers, weeklies, dailies, business journals, nationals, trade papers, etc., which vary in content, size, format and distribution. The principal difference between the two kinds of newspapers is the fact that paid-circulation newspapers have circulation revenues. Paid circulation can be either on a subscription basis or on a single copy basis, such as at newsstands or through coin boxes. In the case of the Booth newspapers, approximately 20 percent of their total revenues come from circulation revenue, as was the case in 1977. In 1977, approximately 85 percent of the circulation revenue was from subscribers; the balance came from single copy sales. Sales to subscribers were, and are, important to the Booth newspapers because subscriber income is regular and predictable.

On May 31, 1977, the paid subscribers of the Booth newspapers consisted of approximately 460,000 particular customers who had requested that one of the Booth newspapers be delivered to a specific address on a regular basis in return for payment of the subscription price. The number of paid subscribers of each of the Booth newspapers was as follows:

[3] Dr. Urban is an expert in the newspaper industry, including, in particular, consumer behavior, market trends, and operational matters, such as strategic planning, financial forecasting, circulation strategy, advertising strategy, and news and editorial content and redesign.

Newspaper	Daily Subscribers	Sunday Subscribers
Ann Arbor	37,743	37,122
Bay City	37,337	36,255
Flint	91,366	91,155
Grand Rapids	120,011	106,859
Jackson	35,711	35,632
Kalamazoo	51,481	52,960
Muskegon	41,203	40,609
Saginaw	49,327	48,942

Stip. para. j. The name and address of each paid subscriber was retained by Booth or on its behalf by persons responsible for delivery of the papers. Stip. para. j.

The parties have agreed that, if the Court determines that the paid subscribers constitute assets which were separate and apart from goodwill and which can be valued separate and apart from goodwill, and if the Court determines that the paid subscribers had useful lives which can be estimated with reasonable accuracy, then the paid subscribers of the Booth newspapers can be depreciated on a straight-line basis over the following useful lives:

Newspaper	Useful Lives of Daily Subscribers	Useful Lives of Sunday Subscribers
Ann Arbor	14.7	14.7
Bay City	22.2	23.4
Flint	18.3	18.5
Grand Rapids	17.7	21.2
Jackson	17.9	18.9
Kalamazoo	17.0	17.6
Muskegon	18.0	16.2
Saginaw	17.4	18.3

Stip. para. k.

A. Limited Life of the Asset

It is undisputed that all the paid subscribers of the Booth newspapers as of May 31, 1977 would, at some point in time, no longer be subscribers. That fact was recognized by those familiar with Booth, by the members of the Newhouse family when they decided that Herald would purchase Booth, and by those familiar with the newspaper industry generally. Subscribers are lost because of death, relocation, lack of reader time or interest, changing lifestyles, and other factors that are beyond the control of the newspapers. Also, subscribers are lost due to dissatisfaction with the product or service and for various other reasons, including competition from other media sources, such as radio, television, magazines and other paid-circulation and/or free-distribution newspapers.

Defendant contends that the number of subscribers of each of the Booth newspapers, both daily and Sunday, increased from 1977 through the present. Even if true, whether or not new subscribers were added after the date of valuation is not relevant to the nature and value of the asset as of May 31, 1977.

The paid subscribers of the Booth newspapers acquired by Herald on May 31, 1977, were not self-regenerating, i.e., there is no automatic replacement for a subscriber who terminates his or her subscription. Although the total number of subscribers may have or has remained relatively constant, the individual subscribers will not and have not remained the same, and those that may or have discontinued their subscriptions can be or have been replaced only through the substantial efforts of the Booth newspapers. Moreover, because subscribers turn over so frequently, newspapers throughout the country must sell many new subscriptions each year just to maintain their total number of subscribers.

The government's contention that such findings are irrelevant is rejected by the court. The relevance of Morning

Ledger's evidence regarding the substantial costs and efforts required to replace lost subscribers demonstrates that the subscribers are not self-regenerating assets. The fact that the expenses that are incurred in maintaining an asset are deductible does not mandate a finding that the asset itself is not depreciable. Notwithstanding the time consuming and expensive efforts made to generate new subscribers, the penetration of the Booth newspapers, i.e., the percentage of total households in their markets subscribing to the newspapers, has declined significantly over the last 20 years.

In 1977 and 1978, Statistical Research, Inc. ("SRI") and Professor Gerald J. Glasser[4] conducted a study of the paid subscribers of the Booth newspapers as of May 31, 1977. Report of Statistical Research, Inc., "Report on the Average Remaining Life of Subscriptions to Booth Newspapers". Using the methodology described by Dr. Glasser and utilized in his study, which relied upon widely accepted statistical techniques, the court finds that the remaining useful lives of the paid subscribers of the Booth newspapers as of May 31, 1977, could be estimated with reasonable accuracy.

Defendant contends that what Dr. Glasser presented to the Court was a mortality table of subscribers *at a particular address*, not a mortality table of the total subscriptions, and that he calculated the mortality table using only the data directly collected in the survey and from no other subscription data, not even data that Booth had already collected. Defendant further urges that Dr. Glasser did not ask the relevant question, "For how long have you been (or intend to be) a subscriber to the newspaper?"

However, because of the stipulation reached by the parties, Morning Ledger need not prove either the specific

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[4] Dr. Glasser is an expert in statistics, including statistical theory, statistical methods and their applications, sampling, data analysis and survey research.

useful lives of the paid subscribers of the Booth newspapers as of May 31, 1977, or that Dr. Glasser has correctly estimated those lives. In light of the stipulation, defendant's argument with regard to Dr. Glasser's estimation of the specific useful lives of the Booth subscribers is wholly irrelevant. Instead, Dr. Glasser's testimony establishes that qualified experts could estimate with reasonable accuracy the remaining useful lives of the paid subscribers of the Booth newspapers as of May 31, 1977.

As to the question asked, Dr. Glasser explained that the same methodology that he utilized, which is generally accepted by statistical experts, could have been utilized in asking a different question, and such a survey would likewise have led to reasonably accurate estimates of the useful lives of the Booth subscribers.

B. Valuing the Asset

There were three basis valuation approaches that might have been utilized to determine the fair market value of the paid subscribers of the Booth newspapers as of May 31, 1977; the market approach, the cost approach, and the income approach.

Subscribers to an ongoing newspaper are not commonly sold except as part of a sale of the newspaper operation. Accordingly, there was insufficient data available to permit use of the market approach to determine the fair market value of the paid subscribers of the Booth newspapers as of May 31, 1977.

Although it was possible to estimate the direct cost of soliciting additional subscribers to the Booth newspapers, those subscribers if obtained were not and would not have been comparable, in terms of life characteristics or value, to the paid subscribers of the Booth newspapers as of May 31, 1977. Furthermore, complete data as to the total cost of obtaining even such marginal subscribers had never been compiled. The cost of generating such marginal subscribers

would not reflect the fair market value of the existing subscribers of the Booth newspapers as of May 31, 1977. Accordingly, the cost approach could not and should not be used to determine the fair market value of the paid subscribers of the Booth newspapers as of May 31, 1977.

In response to the expert opinions submitted by plaintiff, defendants offered experts who were unqualified, valued the wrong asset and utilized inappropriate methodology.[5]

Defendant asserts that the cost approach is the only valid method of determining the value of any asset relating to the subscribers of the Booth Newspapers as of May 31, 1977. The government submitted expert opinion that every household in the Booth markets could have been solicited for a cost of $3,000,000, and that the result would be to reconstruct the exact set of subscribers, and that the actual cost to recreate the set of subscribers would actually be far less since, conservatively, 40% of all subscribers would have initiated their own subscription.

The cost of obtaining subscribers does not equate with their value to the enterprise. The court finds that the income approach is, in fact, what buyers and sellers would utilize to determine the price at which these assets would change hands. The government's contention totally ignores the substantial efforts and expenses that had been invested over the years in establishing those subscriber relationships.

The income approach is commonly used to value intangible assets of a going business, other than goodwill and going concern value. This approach best reflects the method that buyers and sellers would utilize to determine

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[5] Plaintiff has moved to strike the testimony of defendant's experts. Despite the above finding, the court concludes that (there being no jury) no useful purpose would be served in striking such testimony. On appeal, the appellate court will make its own determination as to the qualifications and testimony of defendant's experts.

the price at which such assets would change hands. Plaintiff's experts presented testimony that buyers and sellers would determine the additional value of the Booth newspapers attributable to the existence of the paid subscribers as of May 31, 1977, and, thus, the price to be paid for those subscribers, by calculating the present value of the net revenue stream they would provide over their limited lives, i.e., the subscription revenue less the cost of collecting that revenue. That methodology, they testified, produces the fair market value of the paid subscribers of the Booth newspapers as of May 31, 1977.

Defendant, however, contends that this method does not use a portion of the net income or profit of a business, but rather an entire revenue stream unencumbered or reduced by appropriate costs and expenses, and that the only subtractions from the subscriber revenue stream were the costs associated with delivery and collection.

As such, defendant argues that the income method of valuation as used by plaintiff is unacceptable and the produced values are not persuasive. Defendant contends that there are additional costs which plaintiff never identified or even considered, for instance, an apportioned cost of producing the newspaper, since a sale of a newspaper and the income derived from the sale is not independent of the cost of producing the paper.

During the trial, the court on numerous occasions questioned the propriety of valuing the subject asset without making any adjustments or deductions for production costs, overhead expense, etc. Although the government raises the same questions, it offered no competent evidence to the court upon which the court could base any finding to reduce plaintiff's evidence of valuation. Absent such evidence the court cannot speculate as to what deductions would be appropriate and how they would impact upon the overall valuation. Plaintiff, on the other hand, presented evidence that their experts' methodology was fully in accordance

with generally accepted valuation principles, and the validity of their analysis was supported by the detailed expert testimony of Dr. Urban. Furthermore, Mr. Berkey explained that he had tested his conclusions by a second income approach methodology that included allocating the relevant share of all costs, and that exercise confirmed his initial valuation conclusion. Accordingly the court accepts both the methodology and valuations submitted by plaintiff's experts.

C. Distinguishing Goodwill and Fixing Value

As to whether this is an asset separate and apart from goodwill, "goodwill" is the expectancy that the old customers will resort to the old place. The essence of goodwill is the expectancy of continued patronage, for whatever reason. Goodwill is acquired by the purchase of a going concern where the transfer enables the purchaser to step into the shoes of the seller.

Goodwill, by definition, has an indefinite life and is valued using the residual method. By contrast, the paid subscribers of the Booth newspapers as of May 31, 1977, could be, and were, identified; had limited lives that could be estimated with reasonable accuracy; and could be, and herein have been, valued directly. Moreover, the paid subscribers of the Booth newspapers as of May 31, 1977, were not self-regenerating. Therefore, the paid subscribers of the Booth newspapers as of May 31, 1977, were assets with values separate and apart from goodwill.

As stated at the outset, paid subscribers are distinct from previous customers who may or may not return, who may buy more or less or nothing at all. They are identifiable; how long they will remain as subscribers can be predicted with reasonable accuracy; and their value can be measured with a fair degree of accuracy. It is these unique characteristics which separates them from general goodwill and permits of a separate valuation.

To ascertain the fair market values of the paid subscribers of the Booth newspapers, Morning Ledger's valuation experts, Messrs. Larry D. Berkey and Roger J. Grabowski, used a widely accepted application of the income approach to valuation. Specifically, they computed the present value of the after-tax subscription revenues to be derived from the paid subscribers, less the cost of collecting those revenues, and added the present value of the tax savings resulting from the depreciation of the paid subscribers. Both Mr. Berkey and Mr. Grabowski utilized this method because they each independently concluded that this method best determined the additional value of the Booth newspapers attributable to the existence of the paid subscribers as of May 31, 1977, and, thus, the fair market value of those subscribers. As part of this determination, they each concluded that the only additional category of revenue which would be found in a paid subscription newspaper as compared to a free-distribution newspaper is the subscription revenue; similarly, the only additional category of costs is the cost of collecting that revenue. Mr. Berkey concluded that the aggregate fair market value of the paid subscribers of the Booth newspapers as of May 31, 1977, was $67,773,000, and Mr. Grabowski concluded that the fair market value was $60,470,000. The difference in these two valuation conclusions is attributable to Mr. Berkey's use of a four percent per annum inflation factor that Mr. Grabowski did not apply in this valuation. Mr. Berkey tested and confirmed his valuation conclusion by application of another income method under which the relevant portion of all revenues and costs, including editorial costs, production costs, and overhead, were allocated in the valuation of the paid subscribers as of May 31, 1977. Under that analysis, which Mr. Berkey explained was somewhat conservative, he concluded that the paid subscribers would be determined to have a value of $61,500,000, which supported his valuation conclusion under the preferred method of analysis.

As previously indicated, although the government contested the methodology utilized by plaintiff's experts, it offered no evidence to challenge the accuracy of the methodology utilized. Having concluded that the subscribers had no separate value, or if they did, that the cost of replacing the subscription list was the only appropriate method of analysis, no evidence was presented which would persuade the court that the opinions rendered by plaintiff's experts were inaccurate or invalid.

Based upon the explanation contained in Mr. Berkey's report of the reason why he utilized a four percent inflation factor, and the fact that the government did not challenge that part of Mr. Berkey's methodology and analysis, this court finds that the aggregate fair market value of the paid subscribers of the Booth newspapers as of May 31, 1977, was $67,773,000. The corresponding adjusted tax basis of those subscribers was $71,201,395. See Stip. para. i. The fair market value and adjusted tax basis for each newspaper was as follows:

Subscribers	Number of Subscribers	Fair Market Value	Adjusted Tax Basis
Ann Arbor News—Daily	37,743	3,966,000	4,166,626
Ann Arbor News—Sunday	37,122	557,000	585,177
Bay City Times—Daily	37,337	5,146,000	5,406,318
Bay City Times—Sunday	36,255	737,000	774,282
Flint Journal—Daily	91,366	14,392,000	15,120,040
Flint Journal—Sunday	91,155	1,810,000	1,901,561
Grand Rapids Press—Daily	120,011	13,250,000	13,920,270
Grand Rapids Press—Sunday	106,859	1,761,000	1,850,083
Jackson Citizen Patriot—Daily	35,711	4,622,000	4,855,811

Jackson Citizen Patriot—Sunday	35,632	688,000	722,803
Kalamazoo Gazette—Daily	51,481	6,655,000	6,991,653
Kalamazoo Gazette—Sunday	52,960	1,021,000	1,072,649
Muskegon Chronicle—Daily	41,203	5,116,000	5,374,800
Muskegon Chronicle—Sunday	40,609	651,000	683,932
Saginaw News—Daily	49,327	6,446,000	6,772,080
Saginaw News—Sunday	48,942	955,000	1,003,310
Total		$ 67,773,000	$ 71,201,395

Stip. para. i.

Morning Ledger is entitled to depreciate the adjusted tax bases of the paid subscribers of the Booth newspapers as of May 31, 1977, as determined by this Court, on a straight-line basis over their stipulated useful lives.

To the extent any conclusion of law is deemed to be a finding of fact, it is to that extent hereby made a finding of fact.

Conclusions of Law

This court has jurisdiction of this matter pursuant to 28 U.S.C. § 1346(a)(1). Venue is proper pursuant to 28 U.S.C. § 1402(a)(2).

This matter arises under section 167 of the Code, which provides, in part, that a taxpayer shall be allowed as a depreciation deduction a reasonable allowance for the exhaustion, wear and tear of property used in its trade or business, or of property held by the taxpayer for the production of income. Also relevant is section 1.167(a)-3 of the Treasury regulations, 26 C.F.R. Sec. 1.167(a)-3 at 649 (1988), which provides in pertinent part:

> If an intangible asset is known from experience or other factors to be of use in the business or in the production of income for only a limited period, the length of which can be estimated with reasonable accuracy, such an intangible asset may be the subject of a depreciation allowance. . . . No allowance will be permitted merely because, in the unsupported opinion of the taxpayer, the intangible asset has a limited useful life. No deduction for depreciation is allowable with respect to goodwill.

The standard set forth in section 1.167(a)-3 of the Treasury regulations has evolved into a two-pronged test. To depreciate an intangible asset, a taxpayer must demonstrate as a factual matter that the asset has: a limited useful life, the duration of which can be estimated with reasonable accuracy, and an ascertainable value separate and apart from goodwill. *See, e.g., Donrey, Inc. v. United States*, 809 F.2d 534, 537 (8th Cir. 1987); *Houston Chronicle Publishing Co. v. United States*, 481 F.2d 1240, 1250 (5th Cir. 1973), *cert. denied*, 414 U.S. 1129, 94 S.Ct. 867, 38 L.Ed.2d 754 (1974); *Citizens & Southern Corp. v. Commissioner*, 91 T.C. 463, 479 (1988), *appeal docketed* No. 89-8159 (11th Cir. March 3, 1989); Rev. Rul. 74-456, 1974-2 C.B. 65, 66.

Goodwill is conclusively presumed, per se, not to be depreciable. *Marsh & McLennan v. Commissioner*, 420 F.2d 667, 668 (3rd Cir. 1969); *Winn Dixie Montgomery, Inc. v. United States*, 444 F.2d 677, 683 n. 8 (5th Cir. 1971); *Skilken v. Commissioner*, 420 F.2d 266, 268 (6th Cir. 1969); *Houston Chronicle Publishing Co. v. United States*, supra at 1247; *Am. South Bancorporation v. United States*, 681 F.Supp. 698, 712 (N.D.Ala. 1988).

As the parties have stipulated, the determination is plainly a factual one to be made, in this instance, by the Court. The parties have stipulated that the determination of whether intangible assets, including customer base as-

sets such as Booth's at-will relationships with the paid subscribers of its newspapers on May 31, 1977, have limited useful lives is a factual inquiry. *See, e.g., Richard S. Miller & Sons, Inc. v. United States*, 537 F.2d 446, 452, 210 Ct. Cl. 431 (1976). In this regard, the Treasury regulations require only that the useful lives be estimated with "reasonable accuracy." Treas. Reg. § 1.167(a)-3. As the Fifth Circuit explained in *Houston Chronicle:* "Extreme exactitude in ascertaining the duration of an asset is a paradigm that the law does not demand. All that the law and regulations require is reasonable accuracy in forecasting the asset's useful life." 481 F.2d at 1253-54. *See also Burlington Northern, Inc. v. United States*, 676 F.2d 566, 573, 230 Ct. Cl. 102 (1982); *Richard S. Miller & Sons, Inc.*, 537 F.2d at 455; *Citizens & Southern Corp.*, 91 T.C. at 500; *Liquid Paper Corp. v. United States*, 83-1 U.S.T.C. para. 9305 at 86,779, 2 Cl. Ct. 284 (1983); *Business Service Indus., Inc. v. Commissioner of Internal Revenue*, 51 T.C.M. 539, 543 (1986).

The fair market value of an asset is the price at which the asset would change hands between a hypothetical willing buyer and willing seller, neither being under any compulsion to buy or sell, both parties having reasonable knowledge of relevant facts. Rev. Rul. 59-60, 1959-1 C.B. 237.

Conclusion

Morning Ledger is entitled to depreciate the value of the paid subscribers of the Booth newspapers acquired on May 31, 1977, over their stipulated useful lives, having established that the subscribers have limited useful lives that can be estimated with reasonable accuracy and an ascertainable value separate and apart from goodwill.

To the extent any finding of fact is deemed to be a conclusion of law, it is to that extent hereby made a conclusion of law.

As part of and consistent with these Findings of Fact and Conclusions of Law and any Final Order entered in this matter, the parties are directed to calculate the actual amounts of tax and interest due to Morning Ledger consistent with the Court's findings and opinion.

APPENDIX C

UNITED STATES COURT OF APPEALS
FOR THE THIRD CIRCUIT

NO. 90-5637

NEWARK MORNING LEDGER CO.,
AS SUCCESSOR TO THE HERALD COMPANY,
Appellee

v.

THE UNITED STATES OF AMERICA,
Appellant

(D.C. Civ. No. 88-04836)

SUR PETITION FOR PANEL REHEARING
WITH SUGGESTION FOR REHEARING IN BANC

PRESENT: SLOVITER, *Chief Judge*, BECKER, STAPLETON, MANSMANN, GREENBERG, HUTCHINSON, SCIRICA, COWEN, NYGAARD, ALITO, and ROTH, *Circuit Judges* and SMITH, *District Judge*•

The petition for rehearing filed by appellee, having been submitted to the judges who participated in the decision of this Court and to all the other available circuit judges in active service, and no judge who concurred in the decision having asked for rehearing, and a majority of the circuit judges of the circuit in regular active service not having voted for rehearing by the court in banc, the petition for rehearing is DENIED.

• Honorable D. Brooks Smith, United States District Judge for the Western District of Pennsylvania, sitting by designation.

Judge Greenberg and Judge Nygaard would have granted rehearing.

BY THE COURT:

/s/ Ernest R. Becker
Circuit Judge

DATED: OCT 15 1991